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CIS

DEDUCTIBILITY OF CERTAIN EXPENSES INCURRED BY SELF-EMPLOYED INDIVIDUALS

HEARING

BEFORE THE

SUBCOMMITTEE ON SELECT REVENUE MEASURES

OF THE

COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES

NINETY-SEVENTH CONGRESS

SECOND SESSION

APRIL 19, 1982

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DEDUCTIBILITY OF CERTAIN EXPENSES INCURRED BY SELF-EMPLOYED INDIVIDUALS

MONDAY, APRIL 19, 1982

House of Representatives,
Committee on Ways and Means,
Subcommittee on Select Revenue Measures,
Washington, D.C.

The committee met at 2 p.m., pursuant to notice, in room 1100 of the Longworth House Office Building, Hon. Fortney H. (Pete) Stark (chairman of the subcommittee) presiding.

[Press release announcing the hearing follows:]

[Press release of Tuesday, Apr. 13, 1982]

Hon. Fortney H. (Pete) Stark, Chairman, Subcommittee on Select Revenue Measures, Committee on Ways and Means, Announces a Public Hearing on the Deductibility of Certain Expenses Incurred by Self-Employed Individuals on April 19, 1982

The Honorable Fortney H. (Pete) Stark, Chairman, Subcommittee on Select Revenue Measures, Committee on Ways and Means, U.S. House of Representatives, today announced a public hearing on the deductibility of certain expenses incurred by self-employed individuals on Monday, April 19, 1982. The hearing will begin at 2:00 p.m. in 1100 Longworth House Office Building, the Committee's main hearing room.

Chairman Stark stated in announcing this hearing that "the integrity of our voluntary self-assessment system of taxation depends on the public perception of the equity and efficiency of the system. The Subcommittee hopes to determine what impact the activities of certain self-employed individuals are having on the tax system, particularly, the attempts by certain individuals to deduct large amounts of personal expenses as expenses incurred in carrying on a trade or business."

Testimony will be received from invited witnesses, including the Honorable Roscoe Egger, Jr., Commissioner of the Internal Revenue Service.

BACKGROUND

It has come to the attention of the Subcommittee that certain individuals, particularly those engaged in certain kinds of selling activities, are being advised, and are actually attempting to convert nondeductible personal, living and family expenses into deductible business expenses on the premise that such expenses are ordinary and necessary expenses incurred in carrying on the trade or business of selling. Many of these expenses may be only tangentially related to the individual's selling activities, and in some cases, may greatly exceed the income actually derived from the selling activity. In these situations, the individuals may be able to shelter other income, such as wages or other compensation, with these expenses.

In assisting the full Committee on Ways and Means in carrying out its oversight responsibilities under Rule X of the House, the Subcommittee will investigate the nature and extent of this phenomenon to determine what action, if any, might be necessary to curb this abuse.

Chairman **Stark**. The Subcommittee on Select Revenue Measures will proceed.

For the past several years this subcommittee has been extensively involved in a whole range of issues affecting independent contractors. And today we are holding an oversight hearing because certain compliance problems involving self-employed persons have been brought to the attention of the subcommittee.

The problem we hope to address is whether certain individuals are using their self-employed status to improperly and, in some cases, illegally evade taxation. This problem, however, is not one of concealing income about which we have recently heard so much but rather one of converting personal expenses, such as those for home, meals, travel, entertainment, into business expenses and then using these so-called business deductions to lower taxes on wages or some other source of income.

Evidence has been brought to the attention of this subcommittee that the sellers and distributors of some companies are being aggressively encouraged to engage in a pattern of tax evasion that appears to be growing in scope and in dollars lost to the Treasury. This particular type of activity is being encouraged by certain individuals who, through the use of lectures and tapes exhort sellers of consumer products in the home to convert their personal expenses as deductible business expenses.

The subcommittee has in its possession one such tape recording. The entire tape is over 50 minutes in length and transcripts of the entire tape are available at this hearing. I would like to add at this point that the name of the company, Amway, appears on the cover of the transcript but, to our knowledge, they have no direct or indirect connection with the tape except for the fact that it was received from a person who sells Amway products. And to the extent that that name is on the cover of that transcript the Chair would apologize if it causes the representatives of the Amway Co. any concern. It should not be on there.

I would, however, like to play for you a 5-minute excerpted version of the tape, a transcript of which is also available so that the members of the subcommittee and witnesses and public can get the flavor of the type of scheme that is being advocated. We will play a 5-minute tape at this point. We will make it available to the recorder so she can withhold if she wants at this point.

[Tape being played to hearing.]

Chairman **Stark**. Well, the tape goes on like that at some length and we will hear from a number of witnesses today as we attempt to discern the scope of the problem and what the possible solutions, legislative or otherwise may be necessary.

These types of schemes, be they large or small in scope are of particular concern to us. This problem really threatens our voluntary tax system. There is a spreading cynicism that the tax code favors certain groups over others and only people who could not cheat are those too poor to pay accountants and lawyers to devise tax evasion schemes for them. I believe in the long run we must greatly simplify our tax code while expanding our tax base.

Regardless of inequities in our current code it is the responsibility of this subcommittee to assist in combating tax evasion and fraud. I hope that we will make some progress in that regard in this hearing today. Our first witness today is Mr. Mark L. McConaghy, chief of staff of the Joint Committee on Taxation, who will discuss the present law and, as we call them, some sanitized tax returns.

It is important to stress at this point that no Member of Congress has seen these actual tax returns. They have been provided as completely unidentifiable samples by the Internal Revenue Service and the staff of the Joint Committee on Taxation.

Welcome to the committee, Mark, and you can proceed. I think the members have copies of your letter to me and the summary of the tax returns and they might like to look as you go through your testimony.

The copies of Mr. Mark McConaghy's statement and sanitized returns will be available to the press and interested witnesses.

STATEMENT OF MARK L. McCONAGHY, CHIEF OF STAFF, JOINT COMMITTEE ON TAXATION

Mr. McConaghy. Thank you, Mr. Chairman. I thought it might be helpful to start by summarizing present law relating to trade or business expenses.

Generally, an individual may deduct all ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business. The determination of whether an activity constitutes a trade or business depends on the particular facts involved. Generally, to constitute a trade or business, the activity must be carried on for the likelihood of profit and must occur on a regular basis. In addition, in order to be deductible, the expenses must be ordinary and necessary to the operation of the business and must not be capital items or capital expenditures.

The tax laws also contain three specific limitations on the allowable deduction for expenses claimed to be incurred in business or income-producing activities. First, is what we refer to as the hobby loss provision, section 183 of the code. Under that provision, if an activity is not engaged in for profit, the deduction generally is limited to the income produced from that activity. However, under that section, an activity is presumed to be engaged in for profit if the activity produces net income for any 2 years in a period of 5 successive years.

Second, there is a specific limitation that deals with travel and entertainment expenditures. Section 274 provides that no deduction is permitted for entertainment expenses unless the entertainment is directly related to the active conduct of the taxpayer's business or investment activity.

The third limitation is a combination of the business use of the home and the "vacation home" provisions. That is section 280A. Under that limitation, expenditures attributable to the use of the taxpayer's home are deductible only for that portion of the home that is used exclusively and on a regular basis as a principal place of business of the taxpayer or as a place of business used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of the taxpayer's business.

Also, there is a general provision of the code, section 262, stating that personal, family, or living expenses are not deductible. So, in summary form, I think those essentially constitute the provisions that may relate to the kind of deductions that you asked the staff to look at.

Pursuant to your request, the staff examined Federal income tax returns filed by certain individuals engaged in direct selling activities and has prepared the report which you have in front of you. That report includes examples which reflect income and deductions as shown on actual tax returns. This information has been cleansed so that the information contained is not tax return information.

We examined a number of returns, but I should point out that the returns that we did examine do not represent a valid statistical sample of returns filed by individuals who are engaged in direct selling. These returns, however, illustrate actual situations in which individuals engaged in direct selling activities have reduced the amount of tax liability shown by them on their returns by using deductions claimed to arise from their selling activities to offset wages and other nonbusiness income.

The examples included in the report are taken from a total of 81 tax returns for 1979 or 1980, which were selected from what is called the work-in-progress inventories of three Internal Revenue Service districts.

In general, the returns furnished by the IRS reflect a married couple filing a joint return, three or four personal exemptions, gross wage and salary income in the range of $10,000 to $35,000, total business gross income of less than $5,000, and net business losses of up to $20,000. The categories of business deductions typically claimed on the returns include designations such as automobile and transportation expenditures, entertainment expenses, home meetings, lodging and meal expenses, commissions, demos and samples, awards and gifts, and home office and other office expenses.

Each example of a tax return is divided into three parts. First, we have a summary of income and deductions as shown on the return. Second, we break out and show in detail a composition of the business loss claimed on the return. Third, we show the tax savings which resulted from claiming a net business loss on the return.

I think that the 20 return examples that we have attached to the report pretty much follow the pattern of the 81 returns that we looked at. It may be instructive to go down a few of those examples to get a feel for what they actually show.

We have labeled these examples 1 through 20. In the case of taxpayer No. 1, the first part of the example shows a summary of income and deductions shown on the return. In this case, there were wages of approximately $53,000; total business gross income of about $3,600; a small amount of other income; and total business deductions of $14,651. Also, there were some itemized deductions and personal exemptions, resulting in taxable income of $34,231. The tax shown on the return was $7,800.

Chairman **Stark**. Mark.

Mr. **McConaghy**. Yes, Mr. Chairman?

Chairman **Stark**. Just to repeat. In other words, with the personal exemptions this taxpayer is down to a taxable income of $34,000. The $14,651 of deductions were all business deductions associated with the $3,600 worth of business gross income.

Mr. McConaghy. Yes, Mr. Chairman. These latter amounts were put on schedule C, the trade or business schedule for form 1040. They show $3,591 of gross sales and business deductions of $14,651, for a net business loss of $11,060.

Chairman Stark. I noticed that in a lot of these income compilations in the 20 returns you have zero cost of goods sold which sounds unlikely. In some you may show, for instance, as much as $40,000 of sales with cost of goods sold being almost 80 percent of the gross sales. Is it not likely that that $3,591 is in fact commissions or actually gross profit.?

Mr. McConaghy. Yes, I think it could be one of two things. One is that it could be the net amount after taking out the cost of the goods, or it could be a passthrough item. We were not able to determine that from the face of the returns.

Chairman Stark. Thank you.

Mr. McConaghy. The first example then shows business deductions of $14,651. I might point out the three or four biggest expenses. The largest, of course, is an automobile expense of $4,126. The next largest expense is demos and samples, as the return calls it. The next largest would be tapes and recorders. The next largest would be entertainment expenses. The other claimed deductions vary as we show them by category, the total of which is $14,651.

The second example that we have, taxpayer No. 2, follows that same sort of pattern. There are wages of $23,338. In this case, gross business income is $1,004, and business deductions are $12,703. Taxable income is $10,996, and the tax shown on the return was $1,597. We then break out the composition of the business income which here shows $1,457 in gross sales and cost of goods sold of $453, for total gross business income of $1,004. Total business deductions are $12,703, and the net business loss is $11,699.

The two biggest deduction items on this return that stand out are the "business portion of new car price," which could be questioned, and other automobile expenses of $3,221.

Chairman Stark. Is there any way, Mark, that you can tell from these returns whether in case No. 2, the person would have an automobile anyway? In other words, whether it was a one-automobile family and they were using the automobile for personal use?

Mr. McConaghy. On this return, I guess we cannot, Mr. Chairman. Some of the returns, however, do show that where a family had two automobiles, the expenses attributable to one of them may have been deducted in full. The expenses attributable to the other one may vary, but may be as high as 80 percent.

Chairman Stark. But basically for taxpayer No. 2, from our perspective, you are showing a person with about $1,000 of gross business income. The individual is selling $120 a month of something and grossing about $80 a month, deducting $1,000 a month in a variety of probably noncash expenses and saving taxes of almost $300 a month.

Mr. McConaghy. That is correct.

The third example follows the same sort of pattern. There were wages of $33,781; gross business income of $341; other income of $596; and business deductions of $8,395 that resulted, after itemized deductions and personal exemptions, in taxable income of $16,558. The tax shown on the return was $2,403.

Here, breaking out that business loss, the return showed gross sales of $341 and no cost of goods sold. Of the deductions that were taken on schedule C as business deductions, the largest is automobile expense. In this case, the second largest was seminar expenses of $1,084. The third largest was tapes and recorders. Total business deductions were $8,395, for $8,054 of net business loss.

The fourth example shows wages of $29,432 and other nonbusiness income of $428. This return had $471 of business income, and showed business deductions far in excess of that amount. In this case, $11,434 of business loss produced taxable income of $7,815 and tax shown on the return of $869.

Here, again, when we break out the composition of the business loss, the largest items were one, automobile expenses; two, demos and samples; three, books and literature; four, telephone expenses; and five, tapes and recorders. Also, $671 was deducted for seminars.

Chairman STARK. Mark, without having to go through all 20 of these returns, is there not really a pattern as you just look at 3 or 4 that shows that less than 1 percent, or under 5 percent of the total family income, if these are largely joint returns in gross income, is attributable to the business.

For example, $300, $400 of sales and/or gross business income—$700 to $1,000 a month in deductions. A lot of tax revenues are lost to the Federal Government of $2,000 to $3,000. In many cases, 4, 5, and 10 times the income.

Is that a pattern through all the returns you examined?

Mr. MCCONAGHY. Yes, Mr. Chairman. Such a pattern certainly is representative of the 81 returns that we did look at.

Chairman STARK. These were actual returns?

Mr. MCCONAGHY. Yes, these were actual returns.

Chairman STARK. I think it is important here to note that these returns were not necessarily people affiliated with one particular company, were they?

Mr. MCCONAGHY. That is correct. The 81 returns involved individuals associated with more than one company.

Chairman STARK. Second, you intend as I understand it, to further investigate the possibility that these people may, although it seems unlikely, may all be new people to the business, and you look at some people who have been in this business for several years to see whether there is a pattern of increasing sales.

So that in case we have overlooked the fact that people might in fact be building a business that would provide larger income in the future, your staff intends to look into that?

Mr. MCCONAGHY. Yes, Mr. Chairman. You have asked us to do so, and we have requested further returns for these particular individuals for several prior years, in order to see if there is essentially the same pattern for a period of time.

Chairman STARK. Mr. Martin, do you have questions?

Mr. MARTIN. Thank you, Mr. Chairman.

I am not a member of the subcommittee. I appreciate your courtesy. I wanted to follow up on the point that you were making.

As I look through these 20, Mr. McConaghy, the point that the chairman was making, was that all of them have deductions far in excess of income. Were they selected for that purpose or would you say that if you took any random sample of such personal businesses, all of them are going to show this?

That is 20 out of 20, a high percentage.

Mr. McCONAGHY. Mr. Martin, we asked the Internal Revenue Service to give us what they considered to be examples of items of deduction in the area of selling, although I think it is spreading beyond that area. And I think there were one or two returns that did not have the kind of ratio of deductions to income that exist in these examples. Perhaps when Commissioner Egger testifies as to what he sees going on, he may be able to give you more information on that.

Mr. MARTIN. Did you ask just for returns that showed deductions in excess of income?

Mr. McCONAGHY. No, we did not, Mr. Martin. We asked for returns of individuals who were involved in direct selling activities, as such.

Mr. MARTIN. So that although you said that is not a random sample, of the sample that you got, 2 out of 22 were profitable and 20 out of 22 were not profitable for one reason or another. They might become so in the future or might not become so in the future?

Mr. McCONAGHY. That is correct.

Mr. MARTIN. What do you estimate is the frequency with which those returns show zero cost of goods sold? The chairman was inquiring about that and I was distracted for a moment and did not hear. Seems to me there are only two that showed any cost of goods sold. Those were the ones where the sales were rather large. Does that mean that the cost of the goods sold was borne by the manufacturer and there is no direct cost to the sales agent? Is that because of the commission arrangement?

Mr. McCONAGHY. My guess, Mr. Martin, is one of two things—either most of the business income amounts shown really represent the net, meaning gross sales minus the cost of goods sold, and perhaps were reported that way, or there could be situations where, in fact, that person is taking a commission and reporting it as gross sales without having to actually purchase that amount and have a cost of goods.

Mr. MARTIN. If the sales person is selling items on consignment on which she has not paid anything, then there would be no cost of goods sold?

Mr. McCONAGHY. That is correct.

Mr. MARTIN. They would just take whatever percentage is allowed by the manufacturer or distributor as income without any cost of goods sold.

Mr. McCONAGHY. That is correct.

Mr. MARTIN. Mr. Chairman, I do not have any further questions at this time. Thank you.

Chairman STARK. Mr. Fowler.

Mr. FOWLER. I have no questions.

Chairman STARK. Thank you very much, Mark.

[The staff report of the Joint Committee on Taxation follows:]

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April 16, 1982

Honorable Fortney H. (Pete) Stark
Chairman, Subcommittee on
  Select Revenue Measures
Committee on Ways and Means
Washington, DC 20515

Dear Mr. Chairman:

In announcing a public hearing (to be held April 19) on the deductibility of certain expenses incurred by self-employed individuals, the Subcommittee stated the concern that "certain individuals, particularly those engaged in certain kinds of selling activities, are being advised, and are actually attempting to convert nondeductible personal, living and family expenses into deductible business expenses***." Pursuant to your request in connection with this hearing, the staff of the Joint Committee has examined a number of Federal income tax returns filed by individuals engaged in direct-selling activities and has prepared the attached report.

The report includes examples reflecting income and deductions as shown on actual tax returns. The examples illustrate how some individuals engaged in direct-selling activities have reduced the amount of tax liability shown by them on their returns by using deductions claimed to arise from their selling activities to offset wages and other nonbusiness income. The report also includes a summary of present law on the deductibility of business and investment expenses.

In order to assure the confidentiality of taxpayer information, identification of the particular individuals who filed the returns from which the examples were prepared has been eliminated. In addition, the same general format has been used for all the examples.

Sincerely,

Mark McConaghy

Mark McConaghy

Enclosure

REPORT ON RETURNS OF INDIVIDUALS ENGAGED IN DIRECT-SELLING ACTIVITIES

The staff of the Joint Committee on Taxation has examined a number of 1979 and 1980 Federal income tax returns filed by individuals who are engaged in direct-selling activities. This report describes the returns which were examined and includes examples of income and deductions as shown on 20 such returns.

Confidentiality

Returns were provided to the Joint Committee staff by the Internal Revenue Service pursuant to section 6103(f) of the Internal Revenue Code. The required confidentiality has been assured by eliminating identification of the particular individuals who filed the returns from which the examples were prepared. In addition, the same general format has been used for all the examples. However, each example reflects income and deductions as shown on an actual tax return.

Returns studied

Neither the returns provided to the staff by the IRS nor the examples included with this report represent a valid statistical sampling of returns filed by individuals who are engaged in direct-selling activities. They do, however, illustrate actual situations in which individuals engaged in direct-selling activities have reduced the amount of tax liability shown by them on their returns by using deductions claimed to arise from their selling activities to offset wages and other nonbusiness income.

The examples included with this report are drawn from 81 tax returns selected from the work-in-progress inventories of three IRS districts. The majority of these returns came under examination through the IRS Return Preparers Program. No audit results are available with respect to the returns, because none of the individual examinations have been completed.

Profile of returns

In general, the returns furnished by the IRS reflect a married couple filing a joint return, three or four personal exemptions, gross wage and salary income in the range of $10,000 to $35,000, total business gross income (gross receipts from sales less cost of goods sold) of less than $5,000, and net business losses of up to $20,000. The categories of business deductions typically claimed on the returns include designations as automobile and transportation expenses, entertainment expenses, home meetings, lodging and meals expenses, commissions, demos and samples, awards and gifts, and home office and other office expenses. Other types of expenses claimed on one or more returns include designations as camera expenses, laundry and cleaning, suits, "outside services," household help, and "yard work."

The 20 examples drawn by the staff from the returns generally reflect this pattern.

Explanation of examples

Each example of a taxpayer return is divided into three parts: (1) summary of income and deductions as shown on the return, (2) composition of business loss claimed on the return, and (3) the tax savings resulting from claiming a net business loss on the return.

The first part of each example shows gross income (wages, total business gross income, and other income); adjusted gross income (gross income minus total business deductions); and taxable income (adjusted gross income minus itemized deductions and personal exemptions as shown on the return). The second part includes a detailed listing of categories of claimed deductions that comprise the total business deductions shown in the first part. The final part of each example shows the tax savings that resulted from offsetting the claimed net business losses against wage or other income. This tax savings computation assumes that the individual had sufficient valid business deductions to offset all gross income from the selling activity.

Because the examples are not drawn from a valid statistical sample of returns, any conclusions drawn from a review of them might not be valid generally for the total class of individuals engaged in direct-selling. However, the examples do illustrate how some individuals seek to reduce their tax liability by claiming losses from direct-selling activities to offset their wage and other nonbusiness income.

Taxpayer # 1

A. Summary of Income and Deductions as Shown on Return

Wages	$52,905
Total business gross income	3,591
Other income	789
Gross income	$57,285
Total business deductions	($14,651)
Adjusted gross income	$42,634
Itemized deductions	($6,403)
Personal exemptions	($2,000)
Taxable income	$34,231

B. Composition of Business Loss

Income:

Gross sales	$3,591	
Cost of goods sold	0	
Total gross business income		$ 3,591

Deductions

Automobile expense	$4,126	
Parking fees	80	
Road tolls	0	
Commercial transportation fees	53	
Depreciation expense (office equip.)	334	
Entertainment expense	1,103	
Convention expense	0	
Seminars	168	
Home meetings	211	
Hotel & motel expense	923	
Meals away from home	309	
Tax preparation fee	0	
Rent	112	
Printing expense	220	
Bank charges	36	
Telephone expense	702	
Postage	28	
Office supplies	783	
Freight charges	620	
Commissions paid	699	
Advertising expense	25	
Sales literature	0	
Demos & samples	1,469	
Awards & gifts	21	
Camera expense	149	
Contests	0	
Books & literature	496	
Dues & subscriptions	13	
Tapes & Recorders	1,371	
Home office	500	
Calculator	100	
Total deductions		($14,651)
Net business loss		($11,060)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$12,501
Tax shown on return	7,801
Tax savings	$ 4,700

Taxpayer # 2

A. Summary of Income and Deductions as Shown on Return

Wages	$23,338
Total business gross income	1,004
Other income	357
Gross income	$24,699
Total business deductions	(12,703)
Adjusted gross income	$11,996
Itemized deductions	0
Personal exemptions	(1,000)
Taxable income	$10,996

B. Composition of Business Loss

Income:

Gross sales	$1,457	
Cost of goods sold	(453)	
Total gross business income		$ 1,004

Deductions

Automobile expense	$3,221	
Parking fees	0	
Road tolls	64	
Commercial transportation fees	0	
Depreciation expense	50	
Entertainment expense	0	
Convention expense	0	
Seminars	180	
Home meetings	0	
Hotel & motel expense	324	
Meals away from home	596	
Tax preparation fee	0	
Rent	763	
Printing expense	0	
Bank charges	0	
Telephone expense	318	
Postage	10	
Office supplies	72	
Freight charges	9	
Commissions paid	0	
Advertising expense	0	
Sales literature	85	
Demos & samples	115	
Awards & gifts	0	
Camera expense	71	
Contests	0	
Books & literature	0	
Dues & subscriptions	0	
Tapes & Recorders	418	
Laundry & cleaning	75	
Business portion of new car price	5,864	
Business loss	130	
Misc.	338	
Total deductions		($12,703)
Net business loss		($11,699)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 5,093
Tax shown on return	1,597
Tax savings	$ 3,496

Taxpayer # 3

A. Summary of Income and Deductions as Shown on Return

Wages	$33,781
Total business gross income	341
Other income	596
Gross income	$34,718
Total business deductions	(8,395)
Adjusted gross income	$26,323
Itemized deductions	(6,765)
Personal exemptions	(3,000)
Taxable income	$16,558

B. Composition of Business Loss

Income:

Gross sales	$ 341	
Cost of goods sold	0	
Total gross business income		$ 341

Deductions

Automobile expense	$3,290	
Parking fees	45	
Road tolls	25	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	354	
Convention expense	0	
Seminars	1,084	
Home meetings	158	
Hotel & motel expense	100	
Meals away from home	378	
Tax preparation fee	80	
Rent	273	
Printing expense	39	
Bank charges	0	
Telephone expense	468	
Postage	30	
Office supplies	100	
Freight charges	51	
Commissions paid	0	
Advertising expense	80	
Sales literature	50	
Demos & samples	400	
Awards & gifts	196	
Camera expense	200	
Contests	0	
Books & literature	160	
Dues & subscriptions	10	
Tapes & Recorders	644	
Equipment	180	
Total deductions		(8,395)
Net business loss		($ 8,054)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 4,513
Tax shown on return	2,403
Tax savings	$ 2,110

Taxpayer #4

A. Summary of Income and Deductions as Shown on Return

Wages	$ 29,432
Total business gross income	471
Other income	428
Gross income	$ 30,331
Total business deductions	($11,434)
Adjusted gross income	$ 18,897
Itemized deductions	($ 9,082)
Personal exemptions	($ 2,000)
Taxable income	$ 7,815

B. Composition of Business Loss

Income:

Gross sales	$ 471	
Cost of goods sold	0	
Total gross business income		$ 471

Deductions

Automobile expense	$ 3,025	
Parking fees	212	
Road tolls	0	
Commercial transportation fees	470	
Depreciation expense	82	
Entertainment expense	76	
Convention expense	0	
Seminars	671	
Home meetings	310	
Hotel & motel expense	160	
Meals away from home	24	
Tax preparation fee	0	
Rent	0	
Printing expense	28	
Bank charges	152	
Telephone expense	919	
Postage	16	
Office supplies	545	
Freight charges	172	
Commissions paid	103	
Advertising expense	0	
Sales literature	0	
Demos & samples	1,547	
Awards & gifts	200	
Camera expense	90	
Contests	0	
Books & literature	933	
Dues & subscriptions	13	
Tapes & Recorders	880	
Storage	325	
Misc. expenses	481	
Total deductions		($11,434)
Net business loss		($10,963)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 3,487
Tax shown on return	869
Tax savings	$ 2,618

Taxpayer #5

A. Summary of Income and Deductions as Shown on Return

Wages	$20,095
Total business gross income	5,147
Other income	1,105
Gross income	$26,347
Total business deductions	($21,146)
Adjusted gross income	$ 5,201
Itemized deductions	($ 3,690)
Personal exemptions	(4,000)
Taxable income	$ 0

B. Composition of Business Loss

Income:		
Gross sales	$ 5,147	
Cost of goods sold	0	
Total gross business income		$ 5,147
Deductions		
Automobile expense	$ 6,586	
Parking fees	62	
Road tolls	31	
Commercial transportation fees	0	
Depreciation expense	186	
Entertainment expense	515	
Convention expense	0	
Seminars	682	
Home meetings	848	
Hotel & motel expense	381	
Meals away from home	366	
Tax preparation fee	78	
Rent	0	
Printing expense	5	
Bank charges	74	
Telephone expense	401	
Postage	38	
Office supplies	80	
Freight charges	375	
Commissions paid	4,598	
Advertising expense	82	
Sales literature	526	
Demos & samples	1,836	
Awards & gifts	425	
Camera expense	246	
Contests	0	
Books & literature	67	
Dues & subscriptions	36	
Tapes & Recorders	856	
Home office	1,766	
Total deductions		($21,146)
Net business loss		($15,999)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 1,745
Tax shown on return	0
Tax savings	$ 1,745

Taxpayer # 6

A. Summary of Income and Deductions as Shown on Return

Wages	$47,709
Total business gross income	851
Other income	1,571
Gross income	$50,131
Total business deductions	($8,125)
Adjusted gross income	$42,006
Itemized deductions	($8,854)
Personal exemptions	($3,000)
Taxable income	$30,152

B. Composition of Business Loss

Income:

Gross sales	$ 851	
Cost of goods sold	0	
Total gross business income		$ 851

Deductions

Automobile expense	$ 3,389	
Parking fees	50	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	164	
Convention expense	241	
Seminars	350	
Home meetings	330	
Hotel & motel expense	431	
Meals away from home	216	
Tax preparation fee	100	
Rent	0	
Printing expense	0	
Bank charges	230	
Telephone expense	365	
Postage	3	
Office supplies	241	
Freight charges	26	
Commissions paid	350	
Advertising expense	0	
Sales literature	0	
Demos & samples	390	
Awards & gifts	75	
Camera expense	32	
Contests	0	
Books & literature	85	
Dues & subscriptions	10	
Tapes & Recorders	221	
Equipment	146	
Storage	680	
Total deductions		(8,125)
Net business loss		$(7,274)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 9,119
Tax shown on return	6,303
Tax savings	$ 2,816

Taxpayer # 7

A. Summary of Income and Deductions as Shown on Return

Wages	$19,954
Total business gross income	4,325
Other income	2,285
Gross income	$26,564
Total business deductions	($17,310)
Adjusted gross income	$ 9,254
Itemized deductions	($ 5,396)
Personal exemptions	(1,000)
Taxable income	$ 2,858

B. Composition of Business Loss

Income:

Gross sales	$45,660	
Cost of goods sold	($41,335)	
Total gross business income		$ 4,325

Deductions

Automobile expense	$ 4,199	
Parking fees	0	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	0	
Convention expense	0	
Seminars	0	
Home meetings	0	
Hotel & motel expense	0	
Meals away from home	0	
Tax preparation fee	0	
Rent	0	
Printing expense	0	
Bank charges	0	
Telephone expense	678	
Postage	0	
Office supplies	1,648	
Freight charges	0	
Commissions paid	2,786	
Advertising expense	0	
Sales literature	0	
Demos & samples	0	
Awards & gifts	0	
Camera expense	0	
Contests	0	
Books & literature	0	
Dues & subscriptions	780	
Tapes & Recorders	0	
Utilities	249	
Misc. expenses	6,970	
Total deductions		($17,310)
Net business loss		($12,985)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 2,853
Tax shown on return	81
Tax savings	$ 2,772

Taxpayer #8

A. Summary of Income and Deductions as Shown on Return

Wages	$32,585
Total business gross income	1,004
Other income	6,653
Gross income	$40,242
Total business deductions	($10,378)
Adjusted gross income	$29,864
Itemized deductions	($2,303)
Personal exemptions	($5,000)
Taxable income	$22,561

B. Composition of Business Loss

Income:

Gross sales	$1,004	
Cost of goods sold	0	
Total gross business income		$ 1,004

Deductions

Automobile expense	$1,528	
Parking fees	0	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	1,453	
Convention expense	0	
Seminars	0	
Home meetings	237	
Hotel & motel expense	0	
Meals away from home	0	
Tax preparation fee	0	
Rent	0	
Printing expense	0	
Bank charges	69	
Telephone expense	296	
Postage	7	
Office supplies	11	
Freight charges	0	
Commissions paid	262	
Advertising expense	89	
Sales literature	0	
Demos & samples	1,012	
Awards & gifts	0	
Camera expense	98	
Contests	0	
Books & literature	0	
Dues & subscriptions	70	
Tapes & Recorders	0	
Motor office expenses	3,255	
Home office	937	
Misc. expenses	1,054	
Total deductions		($10,378)
Net business loss		($ 9,374)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 6,950
Tax shown on return	3,938
Tax savings	$ 3,012

Taxpayer # 9

A. Summary of Income and Deductions as Shown on Return

Wages	$18,390
Total business gross income	1,443
Other income	490
Gross income	$20,323
Total business deductions	($13,040)
Adjusted gross income	$ 7,283
Itemized deductions	0
Personal exemptions	($ 2,000)
Taxable income	$ 5,283

B. Composition of Business Loss

Income:

Gross sales	$ 1,443	
Cost of goods sold	0	
Total gross business income		$ 1,443

Deductions

Automobile expense	$ 3,932	
Parking fees	165	
Road tolls	0	
Commercial transportation fees	300	
Depreciation expense	0	
Entertainment expense	43	
Convention expense	261	
Seminars	738	
Home meetings	1,429	
Hotel & motel expense	305	
Meals away from home	636	
Tax preparation fee	90	
Rent	0	
Printing expense	25	
Bank charges	24	
Telephone expense	672	
Postage	56	
Office supplies	103	
Freight charges	255	
Commissions paid	344	
Advertising expense	0	
Sales literature	0	
Demos & samples	1,253	
Awards & gifts	256	
Camera expense	187	
Contests	0	
Books & literature	241	
Dues & subscriptions	94	
Tapes & Recorders	651	
Home office	893	
Equipment	87	
Total deductions		($13,040)
Net business loss		($11,597)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 2,475
Tax shown on return	263
Tax savings	$ 2,212

Taxpayer #10

A. Summary of Income and Deductions as Shown on Return

Wages	$ 19,784
Total business gross income	1,919
Other income	113
Gross income	$ 21,816
Total business deductions	($ 12,351)
Adjusted gross income	$ 9,465
Itemized deductions	($ 3,923)
Personal exemptions	($ 3,000)
Taxable income	$ 2,542

B. Composition of Business Loss

Income:

Gross sales	$ 1,919	
Cost of goods sold	0	
Total gross business income		$ 1,919

Deductions

Automobile expense	$ 5,888	
Parking fees	0	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense)	1,176	
Convention expense)		
Seminars	0	
Home meetings	73	
Hotel & motel expense	0	
Meals away from home	0	
Tax preparation fee	0	
Rent	1,444	
Printing expense	0	
Bank charges	148	
Telephone expense	885	
Postage	46	
Office supplies	950	
Freight charges	192	
Commissions paid	365	
Advertising expense	122	
Sales literature	437	
Demos & samples	234	
Awards & gifts	0	
Camera expense	0	
Contests	0	
Books & literature	0	
Dues & subscriptions	75	
Tapes & Recorders	0	
Insurance	60	
Laundry & cleaning	55	
Legal fees	100	
Misc. expense	101	
Total deductions		($12,351)
Net business loss		($10,432)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 1,630
Tax shown on return	0
Tax savings	$ 1,630

Taxpayer #11

A. Summary of Income and Deductions as Shown on Return

Wages	$30,442
Total business gross income	($2,810)
Other income	10
Gross income	$27,642
Total business deductions	($ 9,716)
Adjusted gross income	$17,926
Itemized deductions	($ 682)
Personal exemptions	($3,000)
Taxable income	$14,244

B. Composition of Business Loss

Income:

Gross sales	$2,507	
Cost of goods sold	5,317	
Total gross business income		($ 2,810)

Deductions

Automobile expense	$2,084	
Parking fees	0	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense) Convention expense)	2,124	
Seminars	0	
Home meetings	0	
Hotel & motel expense	0	
Meals away from home	0	
Tax preparation fee	0	
Rent	1,695	
Printing expense	0	
Bank charges	605	
Telephone expense	217	
Postage	50	
Office supplies	38	
Freight charges	227	
Commissions paid	0	
Advertising expense	0	
Sales literature	0	
Demos & samples	76	
Awards & gifts	0	
Camera expense	0	
Contests	0	
Books & literature	907	
Dues & subscriptions	238	
Tapes & Recorders	0	
Insurance	166	
Laundry & cleaning	66	
Taxes	347	
Utilities	364	
Suits	512	
Total deductions		($ 9,716)
Net business loss		($12,526)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 5,201
Tax shown on return	1,892
Tax savings	$ 3,309

Taxpayer #12

A. Summary of Income and Deductions as Shown on Return

Wages	$ 32,702
Total business gross income	2,129
Other income	801
Gross income	$ 35,632
Total business deductions	($16,858)
Adjusted gross income	$ 18,774
Itemized deductions	($ 7,714)
Personal exemptions	($ 4,000)
Taxable income	$ 7,060

B. Composition of Business Loss

Income:

Gross sales	$ 2,129	
Cost of goods sold	0	
Total gross business income		$ 2,129

Deductions

Automobile expense	$ 6,010	
Parking fees	69	
Road tolls	36	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	0	
Convention expense	415	
Seminars	1,275	
Home meetings	403	
Hotel & motel expense	1,599	
Meals away from home	685	
Tax preparation fee	108	
Rent	0	
Printing expense	106	
Bank charges	19	
Telephone expense	882	
Postage	32	
Office supplies	136	
Freight charges	175	
Commissions paid	1,116	
Advertising expense	0	
Sales literature	0	
Demos & samples	487	
Awards & gifts	15	
Camera expense	596	
Contests	0	
Books & literature	98	
Dues & subscriptions	126	
Tapes & Recorders	1,773	
Storage	500	
Misc. expense	197	
Total deductions		($16,858)
Net business loss		($14,729)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 3,714
Tax shown on return	546
Tax savings	$ 3,168

Taxpayer # 11

A. Summary of Income and Deductions as Shown on Return

Wages	$ 37,498
Total business gross income	2,711
Other income	711
Gross income	$ 40,920
Total business deductions	($14,341)
Adjusted gross income	$ 26,579
Itemized deductions	($ 2,417)
Personal exemptions	($ 4,000)
Taxable income	$ 20,162

B. Composition of Business Loss

Income:

Gross sales	$ 2,711	
Cost of goods sold	0	
Total gross business income		$ 2,711

Deductions

Automobile expense	$ 4,664	
Parking fees	36	
Road tolls	146	
Commercial transportation fees	273	
Depreciation expense	0	
Entertainment expense	567	
Convention expense	273	
Seminars	914	
Home meetings	508	
Hotel & motel expense	303	
Meals away from home	641	
Tax preparation fee	0	
Rent	0	
Printing expense	26	
Bank charges	8	
Telephone expense	683	
Postage	72	
Office supplies	32	
Freight charges	285	
Commissions paid	1,738	
Advertising expense	0	
Sales literature	0	
Demos & samples	1,348	
Awards & gifts	326	
Camera expense	58	
Contests	0	
Books & literature	42	
Dues & subscriptions	34	
Tapes & Recorders	228	
Legal fees	110	
Home office	1,026	
Total deductions		($14,341)
Net business loss		($11,630)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 6,895
Tax shown on return	3,267
Tax savings	$ 3,628

Taxpayer # 14

A. Summary of Income and Deductions as Shown on Return

Wages	$ 0
Total business gross income	2,797
Other income	33,491
Gross income	$ 36,288
Total business deductions	($25,292)
Adjusted gross income	$10,996
Itemized deductions	($ 4,908)
Personal exemptions	($ 4,000)
Taxable income	$ 2,088

B. Composition of Business Loss

Income:

Gross sales	$ 2,797	
Cost of goods sold	0	
Total gross business income		$ 2,797

Deductions

Automobile expense	$ 4,005	
Parking fees	5	
Road tolls	27	
Commercial transportation fees	414	
Depreciation expense (office furn.)	415	
Entertainment expense	1,056	
Convention expense	1,733	
Seminars	84	
Home meetings	820	
Hotel & motel expense	115	
Meals away from home	126	
Tax preparation fee	135	
Rent	0	
Printing expense	149	
Bank charges	124	
Telephone expense	432	
Postage	255	
Office supplies	817	
Freight charges	1,004	
Commissions paid	406	
Advertising expense	0	
Sales literature	606	
Demos & samples	7,559	
Awards & gifts	1,848	
Camera expense	86	
Contests	347	
Books & Literature	0	
Dues & subscriptions	118	
Tapes & Recorders	31	
Home office	1,160	
Interpreting expense	296	
Outside services	1,099	
Total deductions		($25,292)
Net business loss		($22,495)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 4,498
Tax shown on return	0
Tax savings	$ 4,498

Taxpayer # 15

A. Summary of Income and Deductions as Shown on Return

Wages	$33,234
Total business gross income	718
Other income	0
Gross income	$33,952
Total business deductions	($ 8,308)
Adjusted gross income	$25,644
Itemized deductions	($ 4,591)
Personal exemptions	(2,000)
Taxable income	$19,053

B. Composition of Business Loss

Income:

Gross sales	$ 718	
Cost of goods sold	0	
Total gross business income		$ 718

Deductions

Automobile expense	$ 3,936	
Parking fees	46	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	74	
Convention expense	689	
Seminars	259	
Home meetings	0	
Hotel & motel expense	0	
Meals away from home	125	
Tax preparation fee	0	
Rent	0	
Printing expense	0	
Bank charges	0	
Telephone expense	181	
Postage	22	
Office supplies	0	
Freight charges	270	
Commissions paid	23	
Advertising expense	79	
Sales literature	858	
Demos & samples	630	
Awards & gifts	225	
Camera expense	62	
Contests	0	
Books & literature	158	
Dues & subscriptions	7	
Tapes & Recorders	236	
Storage	428	
Total deductions		($ 8,308)
Net business loss		($ 7,590)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 5,153
Tax shown on return	3,003
Tax savings	$ 2,150

Taxpayer # 16

A. Summary of Income and Deductions as Shown on Return

Wages	$11,416
Total business gross income	718
Other income	929
Gross income	$13,063
Total business deductions	($11,391)
Adjusted gross income	$ 1,672
Itemized deductions	($ 2,506)
Personal exemptions	($ 1,000)
Taxable income	$ 0

B. Composition of Business Loss

Income:

Gross sales	$ 718	
Cost of goods sold	0	
Total gross business income		$ 718

Deductions

Automobile expense	$ 6,769	
Parking fees	10	
Road tolls	15	
Commercial transportation fees	606	
Depreciation expense	0	
Entertainment expense	0	
Convention expense	117	
Seminars	155	
Home meetings	702	
Hotel & motel expense	782	
Meals away from home	142	
Tax preparation fee	89	
Rent	0	
Printing expense	0	
Bank charges	18	
Telephone expense	175	
Postage	12	
Office supplies	281	
Freight charges	40	
Commissions paid	230	
Advertising expense	0	
Sales literature	0	
Demos & samples	340	
Awards & gifts	10	
Camera expense	32	
Contests	0	
Books & literature	232	
Dues & subscriptions	10	
Tapes & Recorders	0	
	624	
Total deductions		($11,391)
Net business loss		($10,673)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 1,140
Tax shown on return	0
Tax savings	$ 1,140

Taxpayer #17

A. Summary of Income and Deductions as Shown on Return

Wages	$ 30,160
Total business gross income	1,407
Other income	0
Gross income	$ 31,567
Total business deductions	($14,110)
Adjusted gross income	$ 17,457
Itemized deductions	($ 6,603)
Personal exemptions	($ 3,000)
Taxable income	$ 7,854

B. Composition of Business Loss

Income:		
Gross sales	$ 1,407	
Cost of goods sold	0	
Total gross business income		$ 1,407
Deductions		
Automobile expense	$ 5,472	
Parking fees	0	
Road tolls	0	
Commercial transportation fees	24	
Depreciation expense	293	
Entertainment expense	0	
Convention expense	692	
Seminars	461	
Home meetings	0	
Hotel & motel expense	0	
Meals away from home	0	
Tax preparation fee	30	
Rent	0	
Printing expense	0	
Bank charges	260	
Telephone expense	301	
Postage	85	
Office supplies	915	
Freight charges	0	
Commissions paid	0	
Advertising expense	0	
Sales literature	0	
Demos & samples	1,218	
Awards & gifts	43	
Camera expense	0	
Contests	79	
Books & literature	126	
Dues & subscriptions	97	
Tapes & Recorders	0	
Security system	425	
Insurance	83	
Household help	272	
Yard work	36	
Business debt interest	1,364	
Repairs	66	
Taxes	371	
Utilities	808	
Furniture	689	
Total deductions		($14,110)
Net business loss		($12,703)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 3,378
Tax shown on return	680
Tax savings	$ 2,698

Taxpayer # 18

A. Summary of Income and Deductions as Shown on Return

Wages	$ 33,177
Total business gross income	10,670
Other income	1,595
Gross income	$ 45,442
Total business deductions	($30,576)
Adjusted gross income	$ 14,866
Itemized deductions	($ 7,714)
Personal exemptions	(3,000)
Taxable income	$ 4,152

B. Composition of Business Loss

Income:

Gross sales	$ 10,670	
Cost of goods sold	0	
Total gross business income		$ 10,670

Deductions

Automobile expense	$ 6,665	
Parking fees	0	
Road tolls	0	
Commercial transportation fees	0	
Depreciation expense	0	
Entertainment expense	4,876	
Convention expense	0	
Seminars	0	
Home meetings	364	
Hotel & motel expense	0	
Meals away from home	0	
Tax preparation fee	42	
Rent	1,129	
Printing expense	0	
Bank charges	192	
Telephone expense	438	
Postage	122	
Office supplies	662	
Freight charges	404	
Commissions paid	2,954	
Advertising expense	1,075	
Sales literature	0	
Demos & samples	2,888	
Awards & gifts	0	
Camera expense	0	
Contests	0	
Books & literature	0	
Dues & subscriptions	155	
Tapes & Recorders	0	
Sales & promotion	5,159	
Misc. supplies	331	
Interest	2,498	
Insurance	522	
Legal services	100	
Total deductions		($30,576)
Net business loss		($19,906)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 4,358
Tax shown on return	186
Tax savings	$ 4,172

Taxpayer # 19

A. Summary of Income and Deductions as Shown on Return

Wages	$ 18,208
Total business gross income	2,053
Other income	0
Gross income	$ 20,261
Total business deductions	($15,023)
Adjusted gross income	$ 5,238
Itemized deductions	($ 1,267)
Personal exemptions	($ 4,000)
Taxable income	$ 0

B. Composition of Business Loss

Income:

Gross sales	$ 2,053	
Cost of goods sold	0	
Total gross business income		$ 2,053

Deductions

Automobile expense	$ 8,636	
Parking fees	100	
Road tolls	106	
Commercial transportation fees	356	
Depreciation expense	0	
Entertainment expense	58	
Convention expense	0	
Seminars	126	
Home meetings	104	
Hotel & motel expense	723	
Meals away from home	75	
Tax preparation fee	0	
Rent	0	
Printing expense	0	
Bank charges	52	
Telephone expense	1,456	
Postage	0	
Office supplies	218	
Freight charges	120	
Commissions paid	446	
Advertising expense	17	
Sales literature	49	
Demos & samples	454	
Awards & gifts	32	
Camera expense	72	
Contests	16	
Books & literature	0	
Dues & subscriptions	7	
Tapes & Recorders	488	
Home office	816	
Misc. expense	496	
Total deductions		($15,023)
Net business loss		($12,970)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 1,619
Tax shown on return	0
Tax savings	$ 1,619

Taxpayer #20

A. Summary of Income and Deductions as Shown on Return

Wages	$15,900
Total business gross income	1,155
Other income	0
Gross income	$17,055
Total business deductions	(9,521)
Adjusted gross income	$ 7,534
Itemized deductions	0
Personal exemptions	(2,000)
Taxable income	$ 5,534

B. Composition of Business Loss

Income:

Gross sales	$ 1,155	
Cost of goods sold	0	
Total gross business income		$ 1,155

Deductions

Automobile expense	$ 3,489	
Parking fees	36	
Road tolls	96	
Commercial transportation fees	17	
Depreciation expense	0	
Entertainment expense	343	
Convention expense	0	
Seminars	468	
Home meetings	760	
Hotel & motel expense	293	
Meals away from home	262	
Tax preparation fee	15	
Rent	500	
Printing expense	0	
Bank charges	273	
Telephone expense	1,008	
Postage	24	
Office supplies	209	
Freight charges	79	
Commissions paid	0	
Advertising expense	67	
Sales literature	119	
Demos & samples	219	
Awards & gifts	367	
Camera expense	71	
Contests	63	
Books & literature	197	
Dues & subscriptions	153	
Tapes & Recorders	393	
Total deductions		(9,521)
Net business loss		($ 8,366)

C. Tax Savings Due to Business Deductions

Tax that would have been due without deductions for net business losses	$ 2,206
Tax shown on return	474
Tax savings	$ 1,732

PRESENT LAW ON DEDUCTIBILITY
OF
BUSINESS AND INVESTMENT EXPENSES

Overview

Subject to certain limitations and substantiation requirements, expenses incurred by an individual in carrying on a trade or business are deductible for income tax purposes (Code sec. 162), as are expenses incurred in an investment activity (sec. 212). If the expenses from a business or investment activity exceed the taxpayer's income from the business or investment activity for the year, the net business loss may be used to offset income from other sources, such as employee wages paid to the taxpayer.

Under present law, an activity in which the taxpayer incurs expenditures is presumed to be engaged in for profit (and hence is not subject to the "hobby loss" deduction limitations) if the activity produces net income for at least two years in a period of five consecutive years (sec. 183). Accordingly, as long as an activity shows a profit for any two years within the five-year period, the taxpayer generally may offset income from other sources with excess deductions from the activity in the loss years, unless the Internal Revenue Service can overcome the presumption by establishing that the taxpayer in fact did not engage in the activity for profit.

Except for certain expenses allowed as "above-the-line" deductions or as itemized deductions, an individual's personal or consumption expenditures are not deductible (see sec. 262, disallowing deductions for personal, living, or family expenses). Certain expenditures which otherwise would be treated as personal living expenses, such as expenditures for meals, lodging, travel, or entertainment, nonetheless may be deductible when incurred in a business or investment activity.

Expenses incurred in a trade or business

General rules

An individual may deduct all the ordinary and necessary expenses paid or incurred in carrying on a trade or business (sec. 162).

The determination of whether an activity in which expenditures are incurred constitutes a trade or business depends on the particular facts involved. In general, to constitute a trade or business there must be activities which are carried on for livelihood or profit and which occur on a regular basis. An employee is considered to be in the trade or business of being an employee, and may deduct certain expenses incurred as an employee.[1]

An individual may be engaged in more than one trade or business at a time. Thus, an individual who is an employee may incur deductible expenses from self-employment or investment activities. If the expenses from a business or investment activity exceed the taxpayer's income from that business or investment activity for the year, the net business or investment loss may be used to offset income from other sources, such as employee wages paid to the taxpayer or net income from another trade or business of the taxpayer.

To be deductible, expenses incurred in a trade or business must not be "capital expenditures" and must be "ordinary and necessary" to the operation of the business. In general, a capital expenditure is a cost, other than routine maintenance, incurred for assets or improvements to be used for an extended period. (Such expenditures for business assets, normally may be recovered through depreciation allowances.) As with the definition of trade or business, the determination of whether an expense is ordinary and necessary to the operation of the business is a factual question. The Supreme Court has ruled that expenses do not have to be "habitual or normal in the sense that the same taxpayer will have to make them often" to be ordinary.

Types of deductible expenses

Section 162 specifically lists three categories of trade or business expenditures which are deductible. However, this listing is not exclusive, and other types of trade or business expenses may qualify for deduction pursuant to section 162.

The first listed category of section 162 expenses consists of reasonable allowances for salaries and other compensation for personal services. The principal issue which arises concerning deductions claimed for compensation is whether the total of amounts paid is reasonable in light of the services performed. For example, a corporation may not deduct as compensation amounts paid to a shareholder-employee that are in substance dividends because they exceed reasonable compensation levels. Similarly, an individual operating a business as a sole proprietorship may also violate the reasonableness standard if the individual pays compensation to family members in excess of the value of services in an effort to "income-split" and thereby to maximize the amount of total family income taxable in lower brackets.

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[1] The employee business expenses which are deductible in determining adjusted gross income ("above-the-line deductions") are limited to the following expenses if paid or incurred by the taxpayer in connection with the performance of services as an employee: (1) expenses of travel, meals, and lodging while away from home; (2) other expenses covered by a reimbursement or other expense allowance arrangement with the employer; (3) transportation costs; and (4) expenses of "outside salesmen" (sec. 62(2)). In addition, an individual who itemizes deductions may deduct other employee business expenses (such as union dues or continuing professional education costs).

The second listed category consists of traveling expenses incurred while away from home in pursuit of business. Expenses of commuting to the taxpayer's place of business are nondeductible personal expenses. However, a taxpayer having more than one place of business may deduct the costs of traveling from one place of business to another. In addition, where the taxpayer is away from home in the pursuit of a trade or business, 2/ the taxpayer may deduct traveling expenses, 3/ including the costs of meals and lodging (other than amounts which are lavish or extravagant under the circumstances).

The third listed category of section 162 expenses consists of rentals paid for business property. A deduction may only be claimed for rent which does not exceed the fair market value of

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2/ The travel must be primarily for business purposes. Thus, if a taxpayer makes a business trip (such as attending a convention) and engages in some personal activity such as sightseeing, that part of the total expenses of the trip which is directly attributable to the taxpayer's business is deductible, while expenses attributable to personal activities are nondeductible (Rev. Rul. 79-425, 1979-2 C.B. 81, and Rev. Rul. 56-168, 1956-1 C.B. 93).

3/ If an individual uses an automobile for business purposes (other than for commuting between home and the place of business), he or she may deduct expenses based on a standard mileage rate or based on actual costs incurred. The standard mileage rate is presently 20 cents a mile for the first 15,000 miles, and 11 cents a mile for each additional mile (or for all miles after the car is considered to be fully depreciated, i.e., after 60,000 miles of business use at the maximum rate). The standard rate includes all operating expenses and depreciation allowances.

Alternatively, the taxpayer may elect to deduct automobile expenses based on actual costs incurred and to claim an investment tax credit on the cost of a newly acquired automobile. Deductible expenses under the actual expense method include the cost of gasoline, oil, repairs, insurance, depreciation, licenses, and garage rent.

Parking fees and tolls are deductible separately under both the standard mileage and actual expense methods.

premises actually used for business purposes. In the case of business property purchased by the taxpayer, the cost of the property may be recovered through depreciation deductions.

Expenses incurred for the production of income

A taxpayer may deduct all the ordinary and necessary expenses paid or incurred for production or collection of income; for managing, conserving, or maintaining property held for the production of taxable income; or in connection with the determination of any tax (sec. 212). 4/ These expenses are deductible even though the income-producing activity does not constitute a trade or business under section 162.

Like business expenses, section 212 expenses are deductible only if they are not capital expenditures and are ordinary and necessary expenses to production of the income involved. Thus, the same types of expenses that may be deducted as costs of doing business generally may be deducted when incurred in an investment activity.

Substantiation requirements

Business or investment expenses are generally deductible only if the taxpayer substantiates that he or she actually incurred the expense. If the taxpayer establishes that a deductible expenditure has been incurred, but fails to substantiate the exact amount, the deduction generally may be allowed based on an approximated amount (Cohan v. Comm'r, 39 F.2d 540 (2d Cir. 1930)). However, section 274 requires substantiation of the amount of the expenditure in the case of traveling expenses, entertainment costs, or business gifts (see discussion below).

Limitations on deductible expenses

Present law provides three major limitations on the availability of deductions for expenses claimed to be incurred in business and income-producing activities.

Hobby losses

Hobbies and other activities may resemble business activities although they are not intended to produce a profit. To preclude the claiming of tax losses from such activites to shelter other income, present law restricts deductions in respect of "activities not engaged in for profit" (sec. 183). Under this rule, if an activity is not engaged in for profit, allowable deductions are limited to those amounts which could be deducted without regard

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4/ Expenses incurred for production of tax-exempt income are not deductible (sec. 265).

to the nature of the activity in which incurred (such as certain interest or taxes), plus other expenses in an amount not exceeding the income produced by the activity.

Present law presumes an activity to be engaged in for profit if the activity produces net income for any two or more taxable years in a period of five consecutive taxable years. 5/ Accordingly, so long as an activity shows a profit for any two years within the five-year period, the taxpayer generally may offset income from other sources with excess deductions from the activity in the loss years, unless the Internal Revenue Service can overcome the presumption by establishing that the taxpayer in fact did not engage in the activity for profit. If a particular activity fails to meet the two-of-five-years test, net losses from the activity generally still may be used to offset other income unless the activity is considered not to be engaged in for profit. However, in that case the taxpayer does not get the benefit of the presumption.

If the taxpayer elects, the two-of-five-years determination will not be made before the end of the fourth taxable year, 6/ and the activity will be treated as a business or investment activity until the determination is made. During the period before this determination is made, all deductions otherwise allowable for business or investment expenses can be claimed, subject to later disallowance. Thus, while present law limits deductions when an activity does not have a true profit-making business or investment motive, it permits the taxpayer to defer for up to several years payment of tax on income from other sources to the extent of losses claimed from the activity.

Travel and entertainment expenses

Under section 274, no deduction generally is permitted for expenditures attributable to entertainment unless the entertainment is "directly related to" the active conduct of the taxpayer's business or investment activity; 7/ this requirement is in addition

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5/ In the case of breeding and training race horses, the presumption test is two years of seven consecutive years.

6/ The sixth taxable year in the case of breeding and training race horses.

7/ Entertainment expenses incurred directly before or after a "substantial and bona fide" business discussion are deductible as "associated with" the business even though they are not "directly related to" its conduct. Costs of facilities (e.g., hunting lodges) are considered entertainment expenses.

to the rule limiting all deductible business or investment expenses to those that are ordinary and necessary. In general, entertainment expenses meet the "directly related" test only if (1) the taxpayer expects to derive income or some other specific business benefit (other than goodwill) from the activity; (2) the taxpayer engages in the active conduct of business during the entertainment with the person being entertained; and (3) the active conduct of business is the principal aspect of the combined business and entertainment (Reg. §1.274-2(c)(3)).

Section 274 provides special substantiation requirements for travel and entertainment expenses that are more stringent than the requirements for other types of business and investment expenses. No deduction is allowed for any traveling expense (including meals and lodging while away from home), any entertainment expense, or any business gift expense unless the taxpayer maintains records corroborating the item. 8/ These records must show: (1) the amount of each such expense or other item; (2) the time and place of the travel, entertainment, amusement, recreation, or use of the facility, or the date and description of the gift; (3) the business purpose of the expense or other item; and (4) the business relationship to the taxpayer of persons entertained, using the facility, or receiving the gift.

Business use of home

The tax law imposes limitations on deductions for business use of the taxpayer's home (sec. 280A). A taxpayer may deduct expenses attributable to use of the home for business purposes only for that portion of the home that is used exclusively and on a regular basis as the principal place of business of a trade or business of the taxpayer, or as a place of business used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of the taxpayer's business. Section 280A also contains special rules restricting deduction of expenses incurred in connection with "vacation homes."

Personal, living, and family expenses

In general, personal, living, or family expenses are not deductible in determining taxable income (sec. 262). Examples of such nondeductible expenses are the costs of maintaining a personal residence (e.g., rent, utilities, or depreciation), expenses incurred while traveling away from home (e.g., meals and lodging) to the extent the travel is not primarily for business purposes, expenses of commuting from home to the taxpayer's place of business, and costs incurred for education which does not either maintain or improve skills required in the taxpayer's business or satisfy requirements imposed by the taxpayer's employer.

Present law includes several exceptions to the general rule denying deductions for personal expenses. These exceptions include certain "above-the-line" deductions (e.g., alimony and the deduction for two-earner married couples) and certain itemized deductions (e.g., interest, taxes, casualty losses, charitable contributions, and medical expenses).

8/ Sec. 274 also contains special rules governing expenses of foreign travel and business gifts.

Chairman STARK. Our next witness will be Commissioner Roscoe L. Egger, Jr., Commissioner of the Internal Revenue Service, and he is accompanied by Mr. Fred Williams, the Deputy Assistant Commissioner for Examination, and Mr. Bobby R. Blinson, Chief of Examination of the Baltimore District of the Internal Revenue Service.

I am going to welcome the Commissioner and state for the reporter, Mr. Williams is on the Commissioner's right and on the Commissioner's left is Mr. Blinson, and that we have a prepared statement from Commissioner Egger which will be made a part of the record in its entirety.

Commissioner, you are free to read the statement or summarize it or proceed in any manner you see fit, and I appreciate your taking the time to join us today.

Thank you.

STATEMENT OF ROSCOE L. EGGER, JR., COMMISSIONER, INTERNAL REVENUE SERVICE, ACCOMPANIED BY FRED WILLIAMS, DEPUTY ASSISTANT COMMISSIONER (EXAMINATION), AND BOBBY R. BLINSON, CHIEF OF EXAMINATION, BALTIMORE DISTRICT

Mr. EGGER. I will try to be brief, Mr. Chairman, and not cover the entire statement.

You have already identified the people who are up here with me. I would like to cover a few of the points in my prepared statement.

As you are aware, we recently provided the Joint Committee with selected individual income tax returns which claimed excessive expenses and deductions by individuals engaged in direct selling, as well as a profile of returns as permitted under the Internal Revenue Code 1603(f).

The staff in turn has given you a summary on the data in those returns. I will not be able to comment on any specifics on these returns because of the disclosure provisions of the code. So the testimony here will focus on the general nature of the problem and the actions taken or planned by the Service to explore it in greater depth.

Many individuals engaged in direct selling activities do so part time while they or their spouses are engaged in other income producing activities which constitute their major source of income. While most of these taxpayers are undoubtedly honest, some taxpayers do overstate their expenses, attempting to convert personal expenses into business deductions.

This ultimately results in the sheltering of otherwise taxable income. In essence, these individuals are underpaying their proper taxes through this loss device, causing other taxpayers to bear more than their fair share of the tax burden. The Service views this not only as a serious compliance problem, but a disservice to the country as a whole.

The Service has initiated a dual response to this problem. On the one hand, several of our field offices have undertaken compliance projects on individuals with large business losses on their returns. At the same time, we have established research projects to provide us with a better understanding of the scope and the composition of this problem.

Together, these efforts should provide us the kind of information we need to address the problem in a suitable way.

This general problem, I should mention, touches on a number of other continuing efforts on our part in the compliance area. Specifically, our work on abusive tax shelters, the employee independent contract or status issue, in general, and the tax gap.

For example, our preliminary research into the legal sector of the tax gap indicates that overstated expenses, deductions, and credits of all types amounted to just over $12 billion in 1981, nearly double the amount in 1976 and about 16 percent of the total legal sector tax gap noted from returns filed.

Our final report on the scope and composition of the tax gap will be available this summer.

As I mentioned, the Service is also dealing specifically with this problem through identification and examination of selected individual income tax returns. Although we are still in the early stages of these examinations, it appears that the tax benefit aspects of many of these activities may be the primary reason large numbers of people become involved.

Promotional schemes, recruitment methods and other information we have on these activities frequently highlight the anticipated tax benefits above all else. This indicates to us that the individuals involved know full well what they are doing.

The returns reviewed to date have several common characteristics. Typically, the gross receipts are minimal and often there is a significant loss at the net profit level. Often recorded receipts are from wholesaling where the taxpayer acts as a conduit for other distributors. Since the merchandise being offered frequently is purchased and sold at cost, sometimes no gain results.

In nearly every return, there is a net loss, usually in excess of $1,000. These losses are used to offset wages from the taxpayer's salaried position or income from other sources, resulting in a large tax reduction for the individuals involved.

Some examples of the types of deductions being claimed on these returns may be instructive:

A husband and wife will deduct the cost of many meals eaten out. Since both are officials of the business, these become business meetings.

Taxpayers fragment income within the family structure by paying a minor child to perform chores related to the business. This reduces schedule C income and the child does not have to file a return if paid under the filing requirement of about $3,300.

Taxpayers will take a vacation and deduct the entire cost since they discussed the business with one individual they met on the trip.

Taxpayers have deducted expenses for their pet dogs, since these guard dogs protect the business. This expense item was referred to on the tax return as a security device.

I think you will agree that such expenses are not legitimately deductible and some, in fact, may be so blatant as to call for the imposition of significant penalties in appropriate cases.

In other instances, our review of returns from individuals involved in direct selling has uncovered cases where a taxpayer with $200 in total income claimed a net loss of nearly $5,600 and another where a taxpayer with total income of just under $2,100 claimed net losses of over $24,600. These instances reinforce our belief that compliance in this area is low and in need of attention.

Returns, examined in part in one district have shown average tax deficiencies of between about $1,100 and $1,800 per return. That is somewhere about 2 or 3 times our nationwide experience.

Perhaps more important though is the dreadful indication of the trend of taxpayer compliance. Despite the seriousness of the problems we have described, it is unwise to generalize from these returns about how widespread these abuses may be within this industry or among self-employed taxpayers generally.

We are in the process of defining the full extent of the problem and are not in a position to recommend any legislaton at this point.

However, if our efforts indicate that these practices are widespread or growing, the Congress may wish to consider changes to current law to deal with the problem. In this regard, we are interested in the sorts of proposals advanced by Representative Barber Conable in H.R. 5829, the Taxpayer Compliance Improvement Act of 1982.

Finally, Mr. Chairman, let me say that the Internal Revenue Service views the overstatement of expenses and deductions as a serious problem for both tax revenues and voluntary compliance. Left unattended, this could develop into a threat to the very heart of our self-assessment system of tax administration.

The Service is continuing to work on this problem. We welcome your interest and support and assistance in this effort. My colleagues and I here will be pleased to try to answer any questions that you or members of the subcommittee may have.

[The prepared statement follows:]

STATEMENT OF ROSCOE L. EGGER, JR., COMMISSIONER OF INTERNAL REVENUE

Mr. Chairman and members of the subcommittee, I am pleased to be with you today to discuss some of the problems created by the overstatement of expenses and deductions on certain individual income tax returns which report business receipts from direct sales of consumer products out of the home. With me today are Fred Williams, our Deputy Assistant Commissioner (Examination), and Bobby R. Blinson, Chief, Examination Division in the Baltimore District.

As you are aware, we have recently provided the Joint Committee staff with selected individual income tax returns which claimed excessive expenses and deductions by individuals engaged in direct selling, as well as a profile of the returns, as permitted under Internal Revenue Code Section 6103(f). The staff, in turn, has given you certain summary data on these returns. I will not be able to comment on any specifics of these returns because of the disclosure provisions of the Code, so my testimony here will focus on the general nature of this problem and the actions taken or planned by the Service to explore it in greater depth.

OVERVIEW OF THE PROBLEM

The Internal Revenue Code provides in section 162 that "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business ...." shall be deductible. These expenses are reported to the Service on Schedule C, Profit or Loss from Business or Profession.

Section 162 specifically lists three categories of trade or business expenditures which are deductible. However, this listing is not exclusive, and other types of trade or business expenses may qualify for deduction pursuant to section 162. The first listed category of section 162 expenses consists of reasonable allowances for salaries and other compensation for personal services. The second listed category consists of traveling expenses incurred while away from home in pursuit of business. The third listed category of section 162 expenses consists of rentals paid for business property.

Present law provides three major limitations on the availability of deductions for expenses claimed to be incurred in business and income-producing activities. Under section 274, no deduction generally is permitted for expenditures attributable to entertainment unless the entertainment is "directly related to" the active conduct of the taxpayer's business or investment activity; this requirement is in addition to the rule limiting all deductible business or investment expenses to those that are "ordinary and necessary." The tax law also imposes limitations on deductions for business use of the taxpayer's home (sec. 280A). Finally, personal, living, or family expenses in general are not deductible in determining taxable income (sec. 262).

Of course, business or investment expenses are deductible only if the taxpayer substantiates them as being actually incurred.

Many individuals engaged in direct selling activities do so part-time, while they or their spouses are engaged in other income-producing activities which constitute their major source of income. While most of these taxpayers are undoubtedly honest, some taxpayers do overstate their expenses, attempting to convert personal expenses into business deductions. This ultimately results in the sheltering of otherwise taxable income. In essence, these individuals are underpaying their proper taxes through this loss device, causing other taxpayers to bear more than their "fair share" of the tax burden. The Service views this not only as a serious compliance problem, but a disservice to the country as a whole.

IRS ACTIONS

The Service has practiced a dual response to this problem. On the one hand, several of our field offices have undertaken compliance projects on individuals with large business losses on their returns. At the same time, we have established research projects to provide us with a better understanding of the scope and composition of the problem. Together, these efforts should provide us the kind of information we need to address the problem in a suitable way.

This general problem touches on a number of other continuing IRS efforts in the compliance area, including our work on abusive tax shelters, the employee-independent contractor status issue, and the tax gap. For example, our preliminary research into the legal sector of the tax gap indicates that overstated expenses, deductions, and credits of all types amounted to just over $12 billion in 1981—nearly double the amount in 1976, and about 16 percent of the total legal sector tax gap noted from returns filed. Our final report on the scope and composition of the tax gap will be available this summer. A portion of this effort will address the problem before us today.

As I mentioned, the Service is also dealing specifically with this problem through identification and examination of selected individual income tax returns. Although we are still in the early stages of these examinations, it appears that the tax benefit aspects of many of these activities may be the primary reason large numbers of people become involved. Promotional schemes, recruitment methods, and other information we have on these activities frequently highlight the anticipated tax benefits above all else. This indicates to us that the individuals involved know full well what they are doing.

The returns reviewed to date have several common characteristics. Typically the gross receipts are minimal, and often there is a significant loss at the gross profit level. Often reported receipts are from wholesaling, where the taxpayer acts as a conduit for other distributors. Since the merchandise being offered frequently is purchased and sold at cost, sometimes no gain results. In nearly every return, there is a net loss, usually in excess of $1,000. These losses are used to offset wages from the taxpayers' salaried position or income from other sources, resulting in a large tax reduction for the individuals involved.

Some examples of the types of deductions being claimed on these returns may be instructive:

A husband and wife will deduct the cost of many meals eaten out. Since both are officials of the business, these become "business meetings."

Taxpayers fragment income within the family structure by paying a minor child to perform chores related to the business. This reduces Schedule C income, and the child does not have to file a return if paid under the filing requirement of about $3,300.

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Taxpayers have deducted expenses for their pet dogs, since these "guard dogs" protect the business. This expense item was referred to on the tax return as a "security device."

I think you'll agree that such expenses are not legitimately deductible, and some in fact may well be so blatant as to call for the imposition of significant penalties in appropriate cases.

In other instances, our review of returns from individuals involved in direct selling has uncovered cases where a taxpayer with $200 in total income claimed a net loss of nearly $5,600, and another where a taxpayer with total income of just under $2,100 claimed net losses of over $24,600. These instances reinforce our belief that compliance in this area is low and in need of attention.

Returns examined in part of one district have shown average tax deficiencies of between about $1,100 to $1,800 per return. On a nationwide basis, depending upon the number of returns involved, this could mean a substantial underpayment of taxes. Perhaps more importantly, it is a dreadful indication of the trend in taxpayer compliance.

POSSIBLE LEGISLATIVE SOLUTIONS

Despite the seriousness of the problems we've described, it is unwise to generalize from these returns about how widespread these abuses may be within this industry or among self-employed taxpayers generally. We are in the process of defining the full extent of the problem, and are not in a position to recommend any legislation at this point.

However, if our efforts indicate that these practices are widespread or growing, the Congress may wish to consider changes to current law. In this regard, we are interested in the sorts of proposals advanced by Representative Barber Conable in H.R. 5829, "The Taxpayer Compliance Improvement Act of 1982."

CONCLUSION

Finally, Mr. Chairman, let me say that the Internal Revenue Service views the overstatement of expenses and deductions as a serious problem, both for tax revenues and for voluntary compliance. Left unattended, this could develop into a threat to the very heart of our self-assessment system of tax administration. The Service is continuing to work on this problem, and we welcome your interest, support, and assistance in this effort.

My colleagues and I will be pleased to try and answer any questions you and the members of the Subcommittee may have.

Chairman STARK. Thank you very much, Commissioner Egger.

When you stated that this is one-half to one-third of your problem, is that in relation to $12 billion of overstated expenses and deductions?

Mr. EGGER. I was referring to the dollar amount of the tax deficiencies on examined cases.

Chairman STARK. And do you have an aggregate figure for those?

Mr. EGGER. Not an aggregate. We have no idea how many returns are really involved. At this point we have identified several hundred returns in about three districts and we are just not nearly far enough into the project to be able to identify them.

Chairman STARK. But you mentioned in the tax part of your testimony that you think there are expenses, deductions, and credits that are overstated amounting to about $12 billion. That is in the lost revenue, a part of it is credits, probably?

Mr. EGGER. That's actually loss of tax revenue.

Chairman STARK. That's loss of tax revenue?

Mr. EGGER. Yes, sir.

Chairman STARK. Now, are there data or estimates of what types of deductions, as to how much of this $12 billion might be among the self-employed?

Mr. EGGER. We may be able to furnish some information on that. I do not know whether we have any kind of meaningful breakdown as it might apply to this particular problem. We'll certainly look and see. That number comes from our taxpayer compliance measure in the program and we will have to see what the breakdown is. I just don't know.

[Additional information follows:]

Preliminary estimates of tax revenue loss due to expenses overstated based on 1976 TCMP projected to tax year 1981 [1]

[In millions of dollars]

Type of supporting schedule:	*Revenue loss*
Schedule C, business	4,046
Schedule F, farm	677
Schedule E, rental	697
Partnerships	1,060
Estate and trust income	14
Small business corporations	342
Total	6,836

[1] From preliminary tax gap analysis. These numbers may change when the official report is issued this summer.

Chairman STARK. Although Mr. Blinson accompanies you today, it probably would be unfair to our neighboring city of Baltimore to suggest that this problem lies entirely in the great State of Maryland, and without trying to flag other investigations I have read in newspapers around the country that perhaps in the Midwest and the Far West, these same investigations or same types of problems have appeared, is that correct?

Mr. EGGER. Yes, sir, Mr. Blinson is here because our project in this district is representative of our findings in other districts around the country.

Chairman STARK. Does this problem extend beyond just the individuals in the direct selling area and beyond self-employed individuals?

Mr. EGGER. I can't really be sure of the response to that. For the most part, they are individuals. However, related type problems do exist in other industries but for the most part they would be shown on individual returns because the technique here is to offset other income with business losses.

Chairman STARK. I guess I was thinking in terms of asking you what the next logical type of return would be but it seems to me perhaps salaried and commissioned sales representatives would—it seems to me a little difficult for a craftsman or a service-type person, a plumber or a roof repairperson to make a pretty strong case that every time they go out to dinner, they mention to the waiter that they are a painter or a plumber and therefore are generating business.

Mr. EGGER. They could operate through partnerships or through the 1120S, small business corporations.

Chairman STARK. Even though you can't document the magnitude of this problem, have you a plan or a project that you plan to respond to this problem that you can give us some hint of what you are intending to do?

Mr. EGGER. We are taking several steps. What I would like to do is ask Mr. Blinson if he will give you an overview of what we are doing in his district, and I believe then you can extrapolate that.

Chairman STARK. Fine. Please, Mr. Blinson, proceed.

Mr. BLINSON. In the Baltimore district which, by the way, Mr. Chairman, includes Washington, D.C., as well, we have under examination at the present time approximately 500 returns with another 900 to 1,000 returns identified for possible examination.

So far we have closed approximately 113 returns with results, as the Commissioner indicated, ranging from $1,100 to in excess of $2,000, and in some cases larger.

We have accomplished this with what we consider to be an average time on a case of about 6.9 hours. The results that we have attained on the examination of these returns are around three times the normal result of examinations through our normal system.

Chairman STARK. You mean additional revenue that you collect?

Mr. BLINSON. Yes, sir.

Chairman STARK. You are spending about 7 man hours to review the returns?

Mr. BLINSON. Yes, sir, with about three times the dollar results.

We have just touched the tip of the iceburg in terms of the examination closures at this point so I don't have any better figures. But we do have under review for possible examination within the next year in excess of 2,000 returns just in the Baltimore district.

Chairman STARK. Have you had to cut down your personnel this year or have you got enough people to handle all this work?

Mr. EGGER. No, sir.

Mr. BLINSON. No, sir, we have hopefully good auditing techniques that will allow our people to really conduct these examinations very quickly.

Chairman STARK. Mr. Fowler.

Mr. FOWLER. On that point, Mr. Blinson, is this essentially an enforcement problem?

Mr. BLINSON. Well, any compliance problem is an enforcement problem and I feel that this is a compliance problem when you have personal expenses deducted of this magnitude.

Mr. FOWLER. What I am saying is, do you have enough auditors to handle this? Are you hiring any more auditors to attempt to combat this?

Mr. EGGER. I expect I had better answer that, Mr. Fowler. The answer is that in fiscal year 1983 we have proposed in our budget request to increase our overall staffing in the compliance area by roughly 5,000 positions, principally in the collection and examination areas so that we can step up our compliance activities.

Since we don't know the scope of this problem and we will not know until we have had a chance to push the project considerably deeper in other regions, it's hard to determine just what kind of an enforcement problem it is. It is possible that we would have to be requesting additional resources.

Mr. FOWLER. Well, if a taxpayer had a question about the allowability of some of the deductions that we have been discussing today, how would he or she get an answer to a legitimate question, especially in light of your plans to discontinue the telephone assistance program on September 30?

Mr. EGGER. We have publication 535, which is very explicit on the business expenses and deductability of business expenses. We also have a publication, the number of which escapes me now, for small businesses. We believe that between those two publications, people should, without any great degree of difficulty, be able to come pretty close to the right answers.

Mr. **Fowler**. You are satisfied that publication 535 is sufficiently clear and specific and available to people in this field?

Mr. **Egger**. Yes, sir. With each income tax package that we mail out is a list of publications and those can be secured fairly quickly, if not directly from such sources as the Post Office, certainly from the district offices around the country or by simple letter request.

Mr. **Fowler**. Well, I don't want to let this opportunity go by, Mr. Commissioner, were you here with us to ask you this question. I want to get your thoughts on this question.

In your opinion, what responsibility should the private sector bear in regard to Federal income tax liabilities of their agents or distributors?

For example, I believe present law requires employers to ignore the number of withholding allowances claimed by employees in certain cases. Should private companies that use self-employed taxpayers bear some degree of responsibility for the potential Federal tax liabilities of their independent contractors?

Mr. **Egger**. Well, I think that goes to the whole question of whether there should be withholding because there is already in the law a requirement that income payments such as commissions and fees and that sort of thing be reported to us under our information reporting program. So the next logical step is withholding, which, as I have said many, many times, is far and away more efficient than any information reporting program could possibly be.

Chairman **Stark**. Let me interrupt there if my colleague will yield.

Mr. **Fowler**. Gladly.

Chairman **Stark**. I would like to ask the opinions of all three of you. If we would do withholding or somehow eliminate the overdeduction or overstatement of expenses and credits, which do you think would yield more revenue—in other words, are more people just not reporting income at all, which I assume you would pick up by withholding or reporting? Are we losing more revenue there or do you suspect we are losing more revenue through actual returns that state accurately the amount of income but get a little optimistic or exaggerated or actually take nonexistent expenses on the other side.

I know you can only guess, but which area do you think is perhaps more important?

Mr. **Egger**. Our studies on the tax gap indicate that the overstatement of expenses, deductions of credits counts for about 16 percent of the total tax gap. Therefore, the rest of it, roughly 84 percent, is due to underreporting or nonreporting of income.

Chairman **Stark**. I guess I am thinking, though, now, specifically in relationship to independent contractors field. Where do you think the larger cost would come there?

Mr. **Egger**. I still believe it is probably in the income reporting area. We can give you our preliminary figures on that.

[The following was subsequently received:]

The Service has no current estimate of the amount of the tax gap attributable to independent contractors.

Chairman **Stark**. Mr. Blinson, I know you don't want to disagree with your boss but you have been wading through these figures. Do you have any feelings about it just in the Baltimore district, let's say?

Mr. **Blinson**. No; I have to agree with the Commissioner.

Chairman **Stark**. I withdraw the question.

Mr. **Blinson**. The underreported income problem, of course, is the largest problem we have to deal with from an examination standpoint.

Chairman **Stark**. Mr. Commissioner, I want to come back to Mr. Blinson, to your statement that you seem to feel that most of these claimed deductions are not allowable under the present law. What provisions do you use when you disallow these deductions? In other words, the travel and entertainment substantiation requirements under section 274? The home office limitations in section 280A? The hobby loss rules in section 183?

Mr. **Egger**. Well, we think we don't get to the substantiation or hobby loss rules until first we decide whether the expense truly is ordinary and necessary. In other words, is it necesary to incur $6,000 worth of automobile expenses to make $200 in sales and that kind of thing. So, pretty clearly, we have to get over the ordinary and necessary hurdle first. Then we get to these other areas.

Chairman **Stark**. Mr. Blinson, I don't know whether you had completed telling us what you are doing in the Baltimore district. Did you want to continue?

Mr. **Blinson**. 162 is the code section, is that what you meant?

Chairman **Stark**. I did not know whether we interrupted you a minute ago as you were telling us about your activities in this area.

Mr. **Blinson**. No.

Chairman **Stark**. I have some questions then about that. First of all, do you have any problem conducting these audits? Do the taxpayers, and this is a purely subjective, I guess, observation, do they believe they have done something improper or do you get a high degree of indignation as if these deductions are something they are entitled to?

Mr. **Blinson**. Generally not, Mr. Chairman. These people have got into this business through a promoter and the promoters are very successful in convincing taxpayers that they have a legitimate tax deduction to offset their income, to shelter their other income. They have been instructed and well trained in how to maintain records. The old shoebox theory of dumping large amounts of records on you.

Chairman **Stark**. Does that really scare you if you see somebody come in with a shoebox full of receipts?

Mr. **Blinson**. No, sir, we take the law as it is written that the burden of proof is on the taxpayer to prove deductions. That's the way we approach our audits. We have a taxpayer produce individual items that are claimed on the return as opposed to us wading through them.

If we are looking at the income side, it may be a different approach but from a deduction standpoint, the burden is on the taxpayer.

Most of them have been found to be very cooperative. The preparers that are involved are generally cooperative.

Chairman **Stark**. Do preparers show up for most of these returns or what percentage is done by individuals?

Mr. **Blinson**. Most of the returns are done by preparers and most of the time they do show up for the examination.

Chairman **Stark**. Do you feel that there is any particular pattern of preparers in relationship to the returns you are investigating? Has any question arisen as to whether the preparers may be doing some thing that's in violation of existing tax law?

Mr. **Blinson**. We have some preparers that are under investigation for that purpose. There are preparer penalty laws. We have some that may not be.

Chairman **Stark**. Mr. Martin?

Mr. **Martin**. Thank you very much, Mr. Chairman.

Mr. Commissioner, on page 7 of your statement, the first sentence there you say returns from one district show an average tax deficiency of $1,100 to $1,800 per return. That is an average of all direct sales people?

Mr. **Egger**. Yes.

Mr. **Martin**. You don't mean all returns, because that would be $180 billion.

Mr. **Egger**. That number pertains to the sampling, or the returns that have been selected for examination under this particular project.

Mr. **Martin**. Of people engaged in direct selling only?

Mr. **Egger**. That is correct, yes.

Mr. **Martin**. Earlier in your remarks you estimated a $12 billion tax gap in 1981. Does that include all categories or just direct sales?

Mr. **Egger**. The number is $12 billion, and it pertains to all revenue loss as a result of overstatement of expenses, deductions and credits.

Mr. **Martin**. Just for direct sales?

Mr. **Egger**. No, indeed, across the board.

Mr. **Martin**. That includes contractors, tax shelters, whatever there is?

Mr. **Egger**. Yes.

Mr. **Martin**. What part of that would you say is the subject of this particular discussion?

Mr. **Egger**. I had thought that I was trying to answer that question from the chairman a little bit ago. I don't have that breakdown here. If we have it, I will furnish it. [See table at p. 42.]

Mr. **Martin**. Great. That is all I need on that.

I enjoyed the list of items on pages 5 and 6 that you characterize as expenses that are not legitimately deductible. If they are not deductible, I assume that you disallow them?

Mr. **Egger**. Absolutely.

Mr. **Martin**. I was amused at the guard dog. My poor old dog can't see, can't hear, can't bite very well. He can't even bark. He sneezes when he gets excited, so he wouldn't be qualified. But if someone has a guard dog that is guarding the premises where there is equipment or something outside, then you judge it on merit, you don't just disallow it because it is a guard dog?

Mr. **Egger**. Naturally. We would look into the circumstances.

Mr. **Martin**. When a taxpayer takes a vacation, what would be legitimate? Obviously you are saying you wouldn't allow them to deduct the hotel expenses or resort expenses, but if they do transact business and actually accomplish some business, then you look favorably on that, maybe the travel expenses?

Mr. **Egger**. Of course, if a taxpayer had a legitimate business activity, regardless of whether he was on vacation or where, and incurred expenses related to that activity, then they would be allowable.

Mr. **Martin**. Fine. I wouldn't want us to give an impression that we are imposing this judgment on all people. I would like to discuss the deductions on page 5 and page 6 further.

For example, where you talk about fragmenting income within that family structure. Is it illegitimate to hire one's child? I know it is on government payroll, but can a person hire their child to clean the business premises? Is that illegitimate?

Mr. **Egger**. They can, but the instances we are referring to are where they are pretty much a matter of form and where the purported services we have reason to believe aren't really being performed. They are very superficial.

Mr. **Martin**. I see. If I were operating a business and wanted my child to get the experience of working in that business with me, what would I have to do to prove to you it was a legitimate expense?

Mr. **Egger**. Well, it is not unusual for younger family members to be involved directly in businesses. Age would have a lot to do with it, the nature of the services performed, the time that they could spend considering schooling and all the rest of these things.

It is a pure question of fact as to whether the individuals do it or not. If you did it as one of the tapes suggest, that you might have a 3-year-old dusting the shelves, that is a little bit far-fetched.

Mr. **Martin**. You would want to see that 3-year-old work, wouldn't you? Generally speaking, you don't mean to imply that hiring a minor child—is it under 18 or under 16—is never a legitimate deduction?

Mr. **Egger**. No, I think I made that clear.

Mr. **Martin**. I was getting that impression from what I read. I wanted to clarify that. A husband and wife will deduct the cost of meals. These are just illustrations you have given, for example. You disallow all such meals of husband and wife, or do you allow an annual business meeting or how do you handle such a thing?

Mr. **Egger**. It would seem to me a husband and wife would have ample opportunity to discuss the business affairs without resorting to——

Mr. **Martin**. You are disallowing all that, then, so you don't need legislation to clarify that point?

Mr. **Egger**. That is correct.

Mr. **Martin**. Very good. In looking at the returns you polled on this project, what percentage of them would you say had large deductions which you disallowed? Would you say it was 90 percent of them?

Mr. Egger. Of the 81 returns that are in this project here, I don't know. Bob, maybe you can answer that. Mr. Blinson has more——

Mr. Martin. This was in the Baltimore district project?

Mr. Egger. Yes.

Mr. Blinson. Principally my district represents 60 percent of the 81 returns. Of the returns that are provided, the deductions are somewhere in the neighborhood of $5,000 to $25,000. So, it is an across-the-board sample of the various types.

We would, from an examination standpoint in the districts, have no reason to bring in returns that we do not consider to be an abusive situation for examination.

Mr. Martin. So you are only talking about those that were dressed out with excessive deductions?

Mr. Blinson. That is correct.

Mr. Martin. You are not implying that is a high or low percentage of all people who engage in direct selling?

Mr. Blinson. No.

Mr. Martin. I would hope we wouldn't give the impression, unless we have evidence to back it up, that everybody engaged in direct selling is ripping off the Tax Code. If they are and you have evidence, let's say it. If you don't have such evidence, we ought to be careful we are not smearing people that we shouldn't be.

Mr. Egger. I think I stated in the statement that we certainly aren't attempting to generalize any conclusions at this point. Our work in that area——

Mr. Martin. Yes, sir, I gather you are very conscious of that. I would hope others would be conscious of it, too, including those who are merely observing what we do here today.

Thank you, Mr. Chairman.

Mr. Fowler. Mr. Chairman, along the same line of my friend from North Carolina, is it too naive to suggest since we all seem to admit that, or to know that there are millions of people, Americans, now engaged in direct selling of one kind or another, to publish a booklet on tax tips for direct sellers to counter some of these promotion activities, warn people who want to conduct a legitimate business, door-to-door or from their home, specifically what we expect of them in compliance with the law?

Mr. Egger. Well, that is a very good suggestion, Mr. Fowler. Quite frankly, I hadn't thought about it before, but the idea appeals to me very much.

Mr. Fowler. Well, I am not usually commended by the Commissioner of Internal Revenue, so I certainly am glad I came today. I would appreciate your looking into it.

One other thing. On the last page of your statement you said that you were interested in the proposal, H.R. 5829, advanced by my colleague, Mr. Conable from New York, has introduced the Taxpayer Compliance Improvement Act of 1982.

What is it in that act? Is there anything specifically that relates to the problem we have been discussing that would help you that is contained in his proposal?

Mr. Egger. There are provisions in there with regard to information reporting that may have applicability in either the form as recommended or perhaps some modified form. There are some suggestions for alternative withholding requirements and things of that kind.

We haven't looked at the bill from that standpoint—that is, from the standpoint of either direct sellers or the broader question of independent contractors—but we certainly will be in the near future.

Mr. Fowler. Should there be, would you support, advocate penalties that would apply to taxpayers who overstate their deductions?

Mr. Egger. Well, there already are penalties in the law for willful disregard of law and regulations. Those penalties would be applicable in the typical case. I think one of the difficulties we see in it is that the penalty structure is not quite as effective where we have a return prepared by a third party as to the individual. In other words, the individual thus has some excuse for how the return went out if it was prepared by a professional preparer.

So, we may be looking at the preparer penalty picture to see whether that requires some further modification.

Mr. Fowler. That would be another argument for preparing the kind of booklet I suggested. You would eliminate a lot of excuses on both sides and you could sock it to the preparer if we came up with this kind of result after the service attempted to do everything it could to inform.

Mr. Egger. We believe people hold themselves out as professionals for the purpose of preparation of returns. They ought to have a pretty good idea of what is allowable in the ordinary and necessary business expense area.

Mr. Fowler. Well, we would like—and I am sure Mr. Conable would like, too—any specific suggestions that you have as you go through his proposal.

Mr. Egger. We believe we are just a bit premature——

Mr. Fowler. We will leave the record open.

Mr. Egger [continuing]. At least insofar as the project is concerned, to be able to identify the scope of it, its full extent. As soon as we are further along, though, we will certainly be back in touch.

Mr. Fowler. Thank you, sir.

[The information follows:]

When Mr. Conable's bill was introduced it was identical to Senate bill S. 2198. It is our understanding that the Ways & Means Committee itself is still reviewing Mr. Conable's bill. We are including a copy of Assistant Secretary Chapoton's testimony of March 22, 1982, before the Senate Finance Subcommittee on Oversight of IRS on the Senate bill which may be helpful to Mr. Conable and the Committee in their consideration of H.R. 5829.

STATEMENT OF HON. JOHN E. CHAPOTON, ASSISTANT SECRETARY (TAX POLICY)

Mr. Chairman and members of this committee, I am pleased to be here today to discuss the provisions of S. 2198, the "Taxpayer Compliance Improvement Act of 1982." In general, we view this bill as an important step in reducing the compliance tax gap—which Commissioner Egger has just described.

OVERVIEW

This is a particularly appropriate time to consider steps that might be taken to collect taxes due under existing law which, for a variety of reasons, currently escape collection. I would like to compliment the Chairman and this Committee for holding hearings on the issues presented by the tax gap. I would also like to thank the Chairman and other sponsors of S. 2198 for introducing this measure, which we think takes important steps toward reducing the compliance tax gap as well as preserving the integrity of our voluntary tax compliance system.

The provisions of S. 2198 may be divided into five categories: (1) broadening the scope of and improving the quality of information reporting; (2) reworking the penalty structure of the Internal Revenue Code to correct certain deficiencies, and to deter troublesome and growing abuses that may reflect increasing public acceptance of noncompliance; (3) adjusting the method of computing interest on payments and receipts by the IRS; (4) revising the antiquated rules dealing with voluntary withholding of tax on retirement plan distributions; and (5) ancillary issues, chiefly application of the Paperwork Reduction Act of 1980 to Treasury and IRS. I will discuss each of these provisions in turn.

REPORTING REQUIREMENTS

General

Under existing law, many types of payments are subject to information reporting. Most payments of dividends and interest aggregating more than $10 in a year are required to be reported to the IRS on Form 1099. Copies of Form 1099 are also required to be sent to taxpayers so that they will have the amount of income from each source readily available. The chief class of obligations that is not covered by these reporting rules is obligations of the United States Government (although there is reporting by the Bureau of the Public Debt to IRS on some types of obligations). Payments such as royalties, rents and annuities are subject to information reporting if the payor is engaged in a trade or business, and the payments in a year exceed $600.

Wages paid to individuals are subject to information reporting in addition to withholding of tax at source. The wage withholding system has been in place for almost forty years; the system has long been accepted, and it is generally agreed that the system functions well.

S. 2198 would effect major changes to the tax rules governing information reporting. The thrust of these provisions is to increase the number of transactions subject to information reporting and, in conjunction with certain proposed penalty provisions, to improve the quality and usability of reported information. We recognize that information reporting on taxable transactions is valuable both to the Government—to enable it to check the information reported by taxpayers—and to the vast majority of taxpayers who conscientiously attempt to report all of their income. Time and experience have shown, however, that information reporting is not a panacea: We need only contrast the rate of taxpayer compliance in the wage area, where withholding is generally required, with current levels of compliance in areas where only information reporting is required. It is estimated that wage and salary income, most of which is subject to withholding, is underreported by only 2 or 3 percent; on the other hand, the comparable figure for interest and dividend income, most of which is subject to information reporting only, is between 10 and 16 percent. Twenty billion dollars or more each year in interest and dividend income goes unreported.

There is little question that compliance is substantially higher under a withholding system than under a system of information reporting only. We therefore believe the time has come for imposing withholding on interest and dividend income as long as the costs to withholding agents of implementing this system are not excessive. For that reason, the Administration has proposed withholding on interest and dividends. Thus, while improving and extending the information reporting network is desirable, particularly to the extent that U.S. Government and corporate bearer obligations would become subject to reporting, we believe that the tax gap has grown too large for us to continue to take limited incremental steps toward improved taxpayer compliance in the interest and dividend area.

The balance of the bill's provisions broadening the scope of information reporting call for: (1) reporting on charged tips; (2) reporting by State and local governments on tax refunds; and (3) issuance of regulations requiring reporting by commodities and securities brokers. Let me discuss these proposals in turn.

Charged tips

Employees who receive tips of $20 or more in a month are required under present law to report such tips to their employer. The employer, in turn, is required to report to the IRS (and to the employee) the amount of tips reported by the employee. The employer is similarly obligated to withhold tax on tips reported by the employee.

Tips are clearly compensation and thus constitute taxable income. Current estimates show that employees report less than 20 percent of their tip income. This is simply unsatisfactory taxpayer compliance. S. 2198 would require employers to treat tips that are charged on a credit card, and paid over by the employer to an employee, as wages subject to information reporting. Small employers, who are defined as those who normally had five or fewer employees during the preceding calendar year, would be exempt from this reporting requirement. Since a paper record is already generated by the credit card transaction, there should be little additional paperwork burden as a result of this requirement; it is therefore desirable to impose information reporting in these circumstances.

State tax refunds

Taxpayers are required to include in income the amount of any State or local income tax refund, if the tax was deducted in a prior year, and the deduction gave rise to a tax benefit. Frequently, however, taxpayers fail to include these refunds in income. Doubtless this noncompliance sometimes results from taxpayer ignorance of the requirements of substantive law. In addition, we believe that taxpayers often completely overlook the fact that they received a refund in the prior year, or lack the particulars about the refund when they fill out their income tax returns. S. 2198 would go far to remedy both of these problems. Receipt of information reports from the States and local taxing jurisdictions would heighten taxpayers' awareness that the refunds are taxable. Additionally, the requirement would provide taxpayers with a timely paper record of the information which they require.

Although this provision is clearly desirable from the point of view of Federal tax administration, we must tread carefully in imposing a requirement of even this limited nature on State and local governments, if for no other reason than out of concern for the costs to the States of complying with these new reporting requirements. We note, however, that there has been a proliferation of information exchange agreements between the Federal and State governments. It is anticipated that many States would satisfy their obligations under this provision of S. 2198 by simply providing the information called for by current agreements (although information would also be required to be provided to the individual taxpayer, a practice that is not now in effect). It thus appears that it would not be unduly burdensome to ask the States and local governments to take the further step of insuring that taxpayers have the needed records concerning State tax refunds to complete their Federal tax returns.

Reports by securities and commodities brokers

The tax law has long provided the Internal Revenue Service with authority to require reporting by brokers of the profits and losses and other information concerning their customers. At present, there are no such requirements in effect. S. 2198 would mandate the issuance of regulations requiring information reporting by commodities and securities brokers on capital transactions, as well as the sale or transfer before maturity of any bond or other evidence of indebtedness (other than Treasury Bills or commercial paper sold or transferred by corporations). In its present form, S. 2198 would require that this information be reported only to the IRS, not to the taxpayers involved. In our view, a substantial part of the value of reporting lies in the fact that it informs taxpayers of their taxable income—in this case, gains and losses on securities and commodities transactions. The failure of taxpayers to receive this information could well account for the very high rate of noncompliance—56 percent—for capital transactions generally. If reporting of capital transactions is to be mandated, we hope the Committee will give careful consideration to the desirability of furnishing information to taxpayers as well as the IRS.

In cases where a brokerage house does not possess all of the information necessary for the taxpayer to compute gain or loss on a given item, we would anticipate that regulations would simply require that the brokerage house report the information that it has. For example, in the case of a customer who brings a security to a brokerage house for sale, the brokerage house would report the sale proceeds. While this would not provide full information on the amount of gain or loss from this transaction, it would give the IRS sufficient information, to determine that the full proceeds were correctly reported, and would fully inform the taxpayer of the sale transaction, requiring only that he ascertain his tax basis to report the transaction correctly.

The extremely poor rate of compliance for capital transactions generally leads us to the conclusion that information reporting by securities and commodities brokers is desirable. However, we would like an opportunity to consider certain questions that are raised by this provision. First, we would wish to consider the types of information that would be useful to IRS in improving compliance in this area. Second, we would like to examine the costs both to the brokerage industry and to the IRS of producing information that would be useful to the Government and taxpayers. We look forward to working with you and representatives of the brokerage industry to develop answers to these questions.

Reporting in machine-processable form

S. 2198 would permit the Commissioner to require that tax returns be filed in a machine-processable form, including on magnetic media in the case of a person who is required to file multiple returns. It is substantially simpler and cheaper for the IRS to process documents filed in machine processable form. Many persons filing large numbers of returns now voluntarily report in magnetic form. Reporting on magnetic media is typically no more expensive (and often less expensive) than reporting on paper. At a time when businesses are increasingly relying on computers to perform basic information processing functions, it seems appropriate to confirm that the Commissioner may require reporting in this manner, recognizing that it will be necessary to employ a flexible approach to take into account situations where persons do not have computer capability.

PENALTY PROVISIONS

Penalties in a voluntary tax compliance system must have two basic characteristics. First, the penalties must deter taxpayer behavior that would impair the voluntary tax compliance system; persons who purposely or recklessly fail to comply with the tax law must be subject to sanctions. Second, penalties must take into account, through abatement processes or otherwise, reasonable errors or omissions made in good faith. This second element is particularly important given the degree of complexity of our tax laws.

Although most taxpayers wish to pay their fair share of taxes, there is an institutionalized minority that relies on flaws in the existing penalty structure to avoid taxes. This avoidance results, in part, from the opportunity under current rules to take highly questionable or aggressive positions on tax returns with knowledge that even if the position taken is struck down, no penalty will be imposed on the resulting tax deficiency so long as a "reasonable basis" for the position taken exists. Because only a small percentage of returns are audited each year, these aggressive positions may never be scrutinized or questioned by the Internal Revenue Service (although it is true that IRS audits a relatively high percentage of certain returns based on selection techniques indicating a high probability of a substantial audit adjustment). Thus, the combination of the audit lottery and the absence of effective penalties makes it profitable for taxpayers to reduce their tax liability through aggressive positions on their tax returns which masquerade as good faith constructions of the tax law. Revision of the penalty structure is thus clearly in order.

Some progress has been made in dealing with abusive taxpayer behavior of this sort. An over-valuation penalty was added by the Economic Recovery Tax Act of 1981 to deter taxpayers from claiming exaggerated deductions or credits based on an overstated valuation of property. As structured, the penalty will apply if the claimed value of property exceeds 150 percent of its true value; appraisal reports or opinions of experts will not, in general, prevent application of the penalty.

Audit lottery penalty

S. 2198 would impose an "audit lottery" penalty equal to 10 percent of an understatement of tax liability if the understatement is substantial. A substantial understatement is defined as 10 percent of tax liability, but at least $5,000 for individuals, subchapter S corporations and personal holding companies, and $10,000 for other corporations. In computing the understatement, items giving rise to a deficiency would be treated as having been reported properly and full tax paid thereon if the taxpayer adequately disclosed on the return or an attachment to the return that the reporting of the item was questionable. Thus, taxpayers who are uncertain about the resolution of an issue may continue to take "reasonable basis" positions, just as under existing law. Taxpayers would, however, be required to disclose to IRS the fact that the questionable or aggressive position has been taken or else face the possibility that this penalty would be imposed.

I applaud the sponsors of S. 2198 for squarely facing the difficult issue of overly aggressive returns filed by taxpayers attempting to take advantage of perceived weaknesses in our voluntary compliance system. It is important to reverse the perception among some taxpayers that adopting aggressive tax return positions is necessary or appropriate to avoid "overpaying" taxes relative to other taxpayers. The audit lottery penalty would undoubtedly go far in reducing that perception.

There are certain aspects of this penalty that we believe are in need of careful consideration. Whether adequate disclosure has been set forth in a tax return may be difficult to resolve in certain cases. Also, we wonder if application of the penalty might be inequitable in certain circumstances, such as in the case of ill-informed taxpayers. We would like to work with this Committee to fashion a penalty that would avoid or minimize these difficulties.

Corporate officer/agent fraud penalty

The second penalty measure of S. 2198 that I wish to review in detail is the corporate officer/agent penalty for participation in the tax fraud of a corporation. Under this provision, a corporate officer, director, or employee, as well as a corporate agent, would be liable for a civil penalty equal to 50 percent of an underpayment of tax by a corporation if the corporate officer or agent "knowingly participated" in the fraud. Knowing participation would include direct participation in the fraud by the individual, ordering a subordinate (whether or not the subordinate was employed by the corporation) to participate in the fraud, or knowing of and not attempting to prevent participation in the fraud by a subordinate. However, conduct would constitute "knowing participation" only if the individual knew or should have known that the participation would result in an underpayment of tax.

Under present law, corporate officers are subject to criminal penalties but not civil penalties for participating in the tax fraud of a corporation. Agents who are tax return preparers may be subject to civil liability of $500 for participating in such fraud. The unavailability of civil sanctions against corporate officers for participating in the fraud of a corporation leaves the IRS without an effective civil remedy against corporate officers who engage in conduct constituting tax fraud of a corporation. While a civil fraud penalty may be asserted against the corporation itself, the burden of such a penalty is borne by the shareholders; particularly in the context of a publicly held corporation, the corporate officer might not feel the "sting" of that penalty.

Initially, the issue of the overlap of the return preparer penalties and the corporate officer/agent penalty should be clarified. Presumably, the amount of any corporate officer/agent fraud penalty should be reduced by the amount of any return preparer penalty. Second, we wonder whether a penalty of $100,000, particularly in the case of relatively low-level employees, may be somewhat high. Aside from these issues, however, the penalty is, in our view, soundly conceived. Conduct amounting to tax fraud committed by a person doing business in noncorporate form would give rise to a civil fraud penalty. It is difficult to see why a different result should obtain merely because the business is carried on in corporate form. Therefore, we view the concept of this penalty as a logical and necessary supplement to the Code provisions dealing with tax fraud.

Penalties for failure to file returns or provide taxpayer identification number

The bill provides for a series of revisions to the penalty provisions relating to information reporting, and adds a withholding requirement in the situation where no social security number or other taxpayer identification number is provided to a payor, or where an incorrect taxpayer identification number is provided to a payor, after the IRS has notified the payor that the number is incorrect. Briefly, these provisions are as follows:

Where a person fails (1) to furnish a taxpayer identification number to a payor, (2) to include a taxpayer identification number in a return, or (3) to include the taxpayer identification number of another person in a statement or return filed (e.g., A's failure to include B's social security number on a Form 1099 issued to B), the $5 penalty provided under present law would be increased to $50, with a maximum of $50,000 (increased from $25,000) for all such failures during a calendar year. Where the failure to include another person's taxpayer identification number in a return filed is intentional, the penalty would be $100 per failure, with no limit.

Where a payor fails to file an information return on dividends, interest or other amounts, the penalty would be increased from $10 to $50 per failure, but not to exceed $50,000 (increased from $25,000). If the failure to file such returns is due to intentional disregard of the filing requirements, the penalty would be 10 percent of the amount of the payment (5 percent in the case of reports by brokers).

If a payee fails to provide a taxpayer identification number to a payor, withholding at the rate of 15 percent would be required. Alternatively, if IRS determines that the taxpayer identification number provided to the payor is incorrect, the payor would start withholding upon notice from the IRS that the taxpayer has failed to supply the correct taxpayer identification number. Withholding would continue as long as the taxpayer fails to provide a number, or does not correct an incorrect number.

Persons should not be able to disregard or deliberately avoid information reporting responsibilities with the expectation that a failure to report income will provoke, at most, trivial sanctions. S. 2198 goes far to making the various Code reporting requirements meaningful by generally increasing the penalties for refusals to comply. I would like to comment on two of these penalty provisions.

The minimum penalty of 10 percent of the amount subject to the reporting requirement (5 percent in the case of reports by brokers) where a payor intentionally disregards the filing requirements would in some cases result in a substantial penalty. However, we think significant penalties are appropriate where parties knowingly attempt to subvert the reporting requirements that are crucial to the functioning of our tax system.

Next, let me mention the "penalty withholding" provision. Many information reports which are received either lack a taxpayer identification number altogether, or show an incorrect number. Fully 11 percent of the reports on dividends and interest payments lack this information. These defective reports are in many cases worthless to the Internal Revenue Service; those reports that are corrected are done at very substantial expense. By implementing a system of source withholding on persons who are not willing to provide correct taxpayer identification numbers, this provision will place the onus of correct information reporting on the person best able to insure that the reporting is accurate. We think this is an appropriate and desirable sanction.

Minimum penalty for extended failure to file

Under present law, a person who fails to file a tax return on a timely basis is subject to penalties based on a percentage of the amount of tax due. Thus, where no tax is due, no civil penalty can be assessed. In many cases, IRS finds it necessary to seek out persons who have failed to file their tax returns, in order to obtain such persons' returns. Many of these persons ultimately are entitled to refunds. In those cases, IRS' efforts to compel the filing are not recompensed, except for the value of the right to use the refund without interest expense (assuming IRS pays the refund within 45 days after the return is filed). S. 2198 addresses this problem by imposing a minimum late filing penalty of $100 when a return is filed more than 60 days after the return due date (including extensions).

We have two reservations about this provision. Initially, we are concerned about the effect of codifying a rule allowing late filing by 60 days. Although we recognize that there could be substantial practical problems in applying this penalty without a grace period, we are not persuaded that Code-sanctioned late filing is a desirable rule of law.

Second, we are concerned that application of the penalty could give rise to a perception of government insensitivity in certain cases where a penalty was applied to poorly-informed persons; however, a liberal construction by IRS of the "reasonable cause" exception to the penalty would go far toward allaying those concerns.

Relief from criminal penalty for failure to file estimated tax return where exceptions applicable

Under present law, the obligation to file an estimated tax return, and the criminal sanction for failure to file such a return, are not correlated with the exceptions to the penalty for underpayment of estimated tax liability. Thus, a sanction for failure to file an estimated tax return may exist for a person who would incur no penalty for underpayment of estimated taxes because one of the statutory exceptions is applicable. S. 2198 would conform the rules imposing criminal liability for failure to file a return to the exceptions from liability for underpayment of estimated taxes. We support this provision.

INTEREST COMPUTATION METHOD

S. 2198 provides a number of adjustments to the Internal Revenue Code interest computation provisions, which apply both to interest due to IRS as well as interest due to taxpayers. In our view, these changes are appropriate and welcome.

Compounding of interest

At present, interest under the Internal Revenue Code is computed on a simple rather than a compound basis. Particularly in the case of an underpayment or overpayment that is outstanding for several years, the simple interest computation has the effect of greatly understating the amount of interest due.

For example, 15 percent simple interest for 1 year is equivalent to 14.5 percent interest compounded semi-annually—not a significant difference. However, 15 percent simple interest for 5 years is equivalent to only 11.5 percent interest compounded semi-annually. For 10 years, a compounded rate of 9.4 percent is equivalent to 15 percent simple interest. Thus, for debts outstanding for longer periods, simple interest—even at a high rate—does not provide adequate compensation for the use of money. As a result, the absence of a compound interest rate in the Code discourages prompt settlement of disputes and prompt payment.

S. 2198 would require interest to be compounded semi-annually. This would bring the tax interest computation into line with modern commercial practice, and would insure that both taxpayers and the Government are treated fairly when they are in a position to receive interest payments. This is a change that is long overdue. We do wish to point out, however, that taxpayers who compute their own interest on deficiencies could have some difficulty in doing so when a compound rate is employed. We would like the opportunity to further consider wheather it would be appropriate to use simple interest, rather than a compound interest computation, for deficiencies that are outstanding for a relatively short period of time.

Interest rate adjustments

Under present law, the interest rate applicable to tax deficiencies and overpayments is adjusted each January 1 effective for the ensuing calendar year to a rate equal to 100 percent of the average prime rate in effect during September of the preceeding year, rounded to the nearest full percentage. This rule was adopted as part of the Economic Recovery Tax Act of 1981. Prior to the 1981 Act, the rate was adjusted every two years, based on a rate equal to 90 percent of the prime interest rate.

S. 2198 would provide for semi-annual adjustments to the interest rate, based on the average prime rate charged by banks (rounded to the nearest full percentage) during the six-month period ending three months prior to the date of the change.

Finally, the bill would limit interest on refunds resulting from operating loss and capital loss carrybacks as well as tax credit carrybacks. Under present law, interest on a refund resulting from such a carryback is computed commencing with the first day of the taxable year following the year in which the loss or credit giving rise to the carryback occurs. We understand that some taxpayers might seek to take advantage of this rule, particularly in the context of the current high interest rates applicable to overpayments, to delay filing a refund claim, thereby earning interest on the tax refund in excess of what they might earn at a bank or other financial institution. S. 2198 would provide that interest on an overpayment resulting from such a carryback would be computed from the date on which a claim for refund is filed, except that interest accruing prior to March 12, 1982 would not be affected.

Although we think the tax system should not create artificial incentives to defer filing of a tax refund claim, some persons have asserted that the rule proposed by S. 2198 would unduly restrict the payment of interest to taxpayers who are unable to file their returns, and, therefore, their refund claims, prior to the due date of the return for the loss or credit year. Therefore, we would like to work with this Committee to insure that there would not be inequitable application of this rule in some cases.

WITHHOLDING ON RETIREMENT PLAN AND ANNUITY DISTRIBUTIONS

S. 2198 would impose reporting requirements on employers who maintain qualified pension, profit-sharing, stock bonus and annuity plans and on administrators of such plans; would extend the withholding system to total distributions, and, on a voluntary basis, to periodic payments from qualified retirement plans, individual retirement accounts and commercial annuities; and would reverse the thrust of the current withholding system for distributions by such plans by requiring that a recipient be subject to withholding unless he elects not to have withholding apply. Subject to certain technical changes, we support these provisions of S. 2198.

Current law

The basic principle that underlies the taxation of distributions from qualified retirement plans or commercial annuities is a familiar one: Distributions that exceed the recipient's basis are generally includible in income in the year received. However, the rules for determining the recipient's basis are often complex, and significant exceptions to the general rule exist. As a result, taxpayers often do not understand the extent to which distributions constitute taxable income. The problem is compounded by the current withholding system and exacerbated by inadequate reporting requirements.

Under current law, there is no mandatory or voluntary withholding on total or lump sum distributions. Thus, the recipient of such a distribution may find it necessary either to increase wage withholding or to make estimated tax payments in order to avoid a penalty for underpayment of estimated taxes. In the case of periodic pension or annuity payments, withholding is possible, but only if it is requested by the recipient. Thus the current withholding system is partial, voluntary, and requires an affirmative act by the recipient.

In addition, the present information reporting system is not effective in providing taxpayers and the Internal Revenue Service with the information required to determine tax liability.

Reporting

The pension and annuity reporting requirements contained in S. 2198 would constitute important steps in closing the compliance gap. Under current law, a person who makes pension or annuity payments in excess of $600 or more in a taxable year must report such payments in accordance with Treasury regulations. Lump sum distributions from pension plans and commercial annuities are reported on Form 1099R while Form W-2P is used in the case of periodic payments. These forms are designed to provide taxpayers and the Internal Revenue Service with the information needed to calculate the individual's income tax liability. However, in many cases, the party making the payment has no acccess to the required information. For example, in order to compute the capital gains portion of the recipient's distribution, it is necessary to know when the recipient's plan participation began and when it ended. In most cases, that information is in the possession of the plan administrator, rather than the bank trustee or insurance company making the payments. While employers and plan administrators generally provide recipients with the required information, there is no statutory obligation that they do so. Under S. 2198, plan administrators would be required to provide both the recipients of distributions and the Internal Revenue Service with the information needed to determine income tax liability. We believe it is imperative that such an obligation be imposed on plan administrators, and we therefore support this portion of S. 2198.

Withholding on periodic payments

S. 2198 would also institute a new system of voluntary withholding on periodic benefit payments under qualified plans or commercial annuities. These provisions would apply to typical pension or annuity payments that are made for a specific number of years or over the recipient's lifetime. The taxable portion of these payments, which is the amount attributable to employer contributions, would be subject to withholding as if it were wages.

The withholding system on periodic payments would be voluntary; the recipient could elect on an annual basis not to have withholding apply. Payors would be required to notify recipients of the opportunity to elect out of the withholding system.

We support these measures to make it easier for pension recipients to use withholding and to avoid the obligation to make estimated tax payments and unanticipated tax burdens at the end of the year. However, we have some concern that the notice provisions of the bill may impose undue burdens on plan administrators. We would be happy to work with this Committee to insure that these provisions pose the minimum administrative burden consistent with informing pension recipients of their right not to have withholding apply.

Withholding on total distributions

S. 2198 would also impose withholding on the taxable portion of a "total distribution." A total distribution is a distribution within one taxable year to the recipient of the balance to his credit under an eligible retirement plan or commercial annuity. As with periodic payments, only the taxable portion of the distribution would be subject to withholding. However, unlike withholding on periodic distributions, withholding on total distributions would be mandatory unless the recipient notified the payor that the distribution would be rolled over to an individual retirement account (IRA) or a qualified plan. Further, withholding would be calculated on the basis of the ten-year averaging rules of section 402(e) of the Code. This will generally result in lower withholding than if normal wage withholding tables and computational procedures were used.

We generally support the withholding system that would apply to total distributions. Specifically, we agree that it is appropriate to institute withholding on these payments; we believe that an exception for rollovers must be made; and we believe that use of the ten-year forward averaging rates on total distributions is an appropriate way to minimize overwithholding.

OTHER PROVISIONS

Issuance of regulations

Under S. 2198, the Internal Revenue Code would be amended to require that rules and regulations necessitated by future Code amendments be issued "as soon as possible." I am not certain of the purpose for this provision. I have no hesitancy in saying that Treasury and IRS today issue all regulations "as soon as possible." Continual changes in the law, the need to carefully consider technical and policy issues presented in the interpretation of complex statutory provisions, and the need to carefully consider the views of affected taxpayers, all delay the issuance of regulations. While I share the general concern about the backlog of regulations projects, I am uncertain about the desirability of writing this measure into the public law.

Effective dates

I have not in this statement attempted to systematically comment on the effective date of each of the many provisions of S. 2198. I do wish to note, however, that it appears to us that early effective dates for certain of the provisions—particularly, for example, where new reporting requirements are involved—could create hardships for persons required to comply with the requirements, as well as for the Internal Revenue Service, in preparing to comply with these measures. Just as an example, I note that interest paid after December 31, 1981 on obligations of corporations issued in bearer form would be subject to reporting for the first time. Obviously, it would be difficult to comply with this requirement in many cases.

We would be happy to work with the Committee in devising effective dates for these provisions which adequately take into account practical difficulties which could arise in implementing some of the bill's provisions.

OME oversight

The last provision of S. 2198 that I would like to mention is section 202(b), which would eliminate oversight by the Office of Management and Budget over certain Treasury functions, particularly those discharged by IRS, under the Paperwork Reduction Act of 1980.

The Administration is still considering the application of the Paperwork Reduction Act to Treasury and IRS, and respectfully requests an opportunity to advise the Committee of its views at a later time.

REVENUE ESTIMATES

The Office of Tax Analysis in the Treasury is currently in the process of estimating the revenue effects of the bill's provisions. These estimates are expected to be completed within the next three weeks. We will furnish these estimates for the record as soon as they are available.

Mr. Fowler. That is all I have, Mr. Chairman.

Mr. Martin. Mr. Chairman, I had a further question about problem preparers.

Mr. Egger. Yes.

Mr. Martin. Those who promote excessive deductions, I guess as a way of doing business as tax return preparers, is that what you are saying?

Mr. Egger. Yes.

Mr. Martin. And who presumably are known to your offices as having a poor track record, so that you probably look for their prepared returns first?

Mr. Egger. Well, certainly we, I think, mentioned that in this particular field we have a few that have already come to our attention that are under investigation.

Mr. Martin. So certainly any return you have that is prepared by such a preparer raises a flag with you. What I am getting at is, How do you raise that flag with the taxpayer? Let's presume that a taxpayer wishes to operate a business in a legitimate manner and seeks help, and somebody recommends such a preparer. The taxpayer isn't going to know that that preparer routinely or customarily makes excessive recommendations and so mistakenly relies on it.

Suppose there is such a taxpayer who is trying to start up an honest business and is getting advice and relies on that advice as though that must be the way to do business? Is there any way you can share with the taxpayer the list of those preparers who are subject to——

Mr. **Egger.** No; under present law we would be precluded from making that information known to another taxpayer.

Mr. **Martin.** So the only remedy——

Mr. **Egger.** Is to be aware directly; yes.

Mr. **Martin.** Then the taxpayer ends up paying more taxes, but not being subjected to a penalty?

Mr. **Egger.** That is the typical result; yes.

Mr. **Martin.** Thank you, Mr. Chairman.

Chairman **Stark.** Thank you.

Mr. Williams, do you want to disagree with your boss or add anything?

Mr. **Williams.** No, Mr. Chairman. I agree with Mr. Blinson, who agreed with the Commissioner.

Chairman **Stark.** OK. I want to thank you very much for taking the time and look forward to working with you, Mr. Commissioner, as we proceed through the legislative review of this matter.

Mr. **Egger.** Thank you very much, Mr. Chairman.

Chairman **Stark.** Our next witness is Mr. Alan Fields. Is he in the room?

Mr. **Fields.** Good afternoon, Mr. Chairman.

Chairman **Stark.** Welcome to the committee, Mr. Fields. We appreciate your taking the time to leave that gorgeous California weather and joining us here in Washington.

I know you are accompanied. Would you care to introduce for the reporter the person accompanying you?

Mr. **Fields.** This is Mary L. Sprouse, general counsel of Alan Fields & Associates.

Chairman **Stark.** I would also advise you that these microphones are not very sensitive. To be heard by the reporter and members of the committee, you practically have to swallow them. So, if you wouldn't mind pulling them up close to you, it would help us.

You have submitted to us, Mr. Fields, a statement. It will appear in the record in its entirety, and you may read it for the committee or summarize it or add anything else as you would see fit.

Mr. **Fields.** Yes, Mr. Chairman. I would like to read it, with a couple of additions.

Chairman **Stark.** Go right ahead.

STATEMENT OF ALAN FIELDS, ALAN FIELDS & ASSOCIATES, SHERMAN OAKS, CALIF.

Mr. **Fields.** Mr. Chairman and members of the committee, my name is Alan Fields. I am president of Alan Fields Associates, a tax preparation and audit representation corporation based in Sherman Oaks, Calif.

I am a former IRS agent, hired by the IRS in August 1974. I spent 5½ years with Internal Revenue, 6 months as a revenue representative, 2 years as a tax auditor, and 2 years 10 months as a revenue agent. I resigned from the IRS in December 1979.

In March 1980 I was asked to present a tax seminar. It is my understanding that I have been invited here to discuss with the committee the contents of a tape recorded without my permission at that seminar, over 2 years ago.

Although I consider myself to have an excellent tax background—I am sure Commissioner Egger would agree that the training received over a 5½-year period with the IRS is of high quality—at that time I had no experience in speaking before large audiences.

I was extremely nervous and distraught at the idea of giving that seminar and, in fact, drank almost an entire bottle of Kaopectate that morning. I would be the first to admit that some of the comments made during that seminar show an immaturity and naivete in speaking before an audience.

The audience for that seminar was a select group of active direct salespeople. My remarks were not intended to nor did they apply to the general public or to direct salespeople who are not actively promoting or building their business.

Although I was aware that several members of the audience had tape recorders, I did not realize that tapes of the seminar would be duplicated or distributed. I certainly never foresaw the exposure or publicity the tape has received. Neither myself nor the corporation of which I am president has ever profited directly from the sales of that tape.

I am aware that this tape has been used for purposes I personally never intended nor condoned. Although I stand behind the legitimacy of the deductions outlined in that seminar for direct salespeople actively building their businesses, I realize that the tone and the manner in which the deductions were presented too easily lend themselves to misinterpretation. I am disturbed that in a few instances this has led to misapplication of the tax law.

I have since gone to great expense to counteract and to correct any misconception the tape may have given rise to. I have personally given over 25 seminars and the associates in my firm over 600 free tax workshops in order to educate direct sales people of their true tax obligations.

I have also published a newsletter stating forth in frank and clear language the legitimate tax deductions an active direct salesperson may claim, stressing the business intent and activity necessary to qualify for those deductions. In fact, I would like to quote from my May 1981 newsletter, almost 1 year ago; where I state:

> It continues to be brought to our attention that there are still some distributors that promote their business as a tax shelter. I want to emphatically state, as I have done before at seminars, that your business is not a tax shelter but a business with fantastic income potential. Because of this income potential, those distributors who are actively building their businesses will gain some very substantial tax benefits. Just remember that the best way to get tax benefits from your business is to keep sponsoring and retailing.

My experiences operating a tax firm and in giving tax seminars in the more than 2 years since the recording of that tape have given me an insight into the correct and legitimate tax benefits of a direct sales business.

I do not consider myself a self-appointed tax expert. As a former IRS agent and as an independent Amway direct distributor, I believe I am uniquely qualified to address this area of the tax law.

My purpose in accepting the committee's invitation was to have the opportunity to set the record straight as to my involvement in the matter being studied and to help insure that valid tax deductions will not be eliminated for those who are truly and actively building their direct sales businesses.

I long ago recognized that the original seminar could give rise to misinterpretation, and I have worked diligently and in all good faith to the best of my limited financial resources to correct any misinterpretations the tape has caused.

Though my last 2 years have been spent in the area of management rather than the area of tax preparation, I will be happy to answer any questions that you have.

Thank you for allowing me the opportunity to make this statement.

Chairman **Stark**. Thank you very much, Mr. Fields. I have a couple of questions.

I gather what you are saying is that the tape we heard excerpts of today was to a group of people at a seminar where most of them would have had substantially more than $1,000 or a couple thousand dollars a year in gross income. These were more successful, businesswise.

Did you have a chance to look through the 20 returns?

Mr. **Fields**. Yes, I did.

Chairman **Stark**. They had much higher gross incomes than was evidenced by the returns Mr. McConaghy represented? Would that be your understanding?

Mr. **Fields**. I did not have access to their returns, but that is my understanding.

Chairman **Stark**. Is what you are suggesting that probably in a bit of enthusiasm part of the income that those people in your audience earned is by recruiting other sales people? Is that correct?

Mr. **Fields**. That is correct.

Chairman **Stark**. They used your tape you are afraid, or some of them did, not for preparing returns but to go out and encourage people to sell for their own reasons? To sell because it is a good tax dodge rather than to sell because there should be good income from making a business profit?

Mr. **Fields**. I don't know if that was their reason.

Chairman **Stark**. You suspect that maybe happened?

Mr. **Fields**. That is possible.

Chairman **Stark**. That is the wrong reason to do this you are saying, and the right reason is to get into the business to make a profit.

Mr. **Fields**. That is correct.

Chairman **Stark**. That is what I thought you were saying in your testimony. I ask this in all candor, but I know you were an Amway distributor, so in May of 1981 you talk about sponsoring and retailing. In your tape in its entirety, I have heard statements. Did you mostly do tax preparing and seminars with Amway distributors, or did you deal with other direct selling people as well?

And I can understand that you might have done it only with Amway as an Amway distributor yourself. That is maybe how you ran into them.

Mr. FIELDS. I had left Internal Revenue Service in December 1979. This was March 1980, so I had not done any preparing of tax returns in any prior years.

Chairman STARK. I guess I am just trying to find out whether you got into the direct selling business as an adjunct to your tax preparing, or preparing business, or if it is because you were doing a lot of preparing for Amway distributors and you decided it was a good business and decided to get into it yourself. I am just curious as to the relationship.

Mr. FIELDS. I joined as an Amway distributor while I was still working for Internal Revenue Service. And I joined for the purpose of earning additional income for my family.

Chairman STARK. OK. Mr. Fowler. Excuse me. Mr. Martin, did you have some questions?

Mr. MARTIN. I do, Mr. Chairman, but if Mr. Fowler has to go, that would be fine.

Mr. FOWLER. Thank you, Mr. Martin.

Mr. Fields, I want to pursue the chairman's line. How long did you work for the Internal Revenue Service?

Mr. FIELDS. I worked for Internal Revenue Service for 5 years 4½ months.

Mr. FOWLER. I believe you said in your statement that the expertise that you gained on tax matters was primarily derived from your work with the IRS, did you not?

Mr. FIELDS. That is correct.

Mr. FOWLER. Do you think you would have been asked in March 1980 to present a tax seminar if you had not gotten that expertise from your employment with the Internal Revenue Service?

Mr. FIELDS. Possibly not.

Mr. FOWLER. Had you ever conducted a tax seminar before?

Mr. FIELDS. That was the first tax seminar.

Mr. FOWLER. Did you tell them at that tax seminar that you were a former agent of the Internal Revenue Service?

Mr. FIELDS. Yes, I did.

Mr. FOWLER. Do you believe that having had that expertise gained from the employment with the Internal Revenue Service that that would incur upon you a responsibility above that of the ordinary citizen to present tax facts and advice accurately, since you were advertising your expertise before that seminar as having come from the Internal Revenue Service?

Mr. FIELDS. It is my belief that all tax areas covered in that seminar have a basis in both case law and in the IRS Code. The seminar was not aimed at other than the people at that seminar.

Mr. FOWLER. Let's see what you say here. Did you make the tape that we heard?

Mr. FIELDS. No.

Mr. FOWLER. Let's put it another way. Are you the voice we heard on that tape?

Mr. FIELDS. Yes.

Mr. FOWLER. You knew what I was talking about, didn't you?

Mr. FIELDS. Pardon?

Mr. FOWLER. On that tape you said,

> Since all of your friends and relatives are either potential prospects or clients or currently prospects or clients, almost any time you go out with a friend or relative

> you can convert that to a business expense if you will just talk business during part of the evening.

Is that the law? Was that the law in March 1980, and is that the law now, Mr. Fields?

Mr. **Fields**. That is the law per Internal Revenue Code section 162, so long as there is a bona fide business relationship.

Mr. **Fowler**. The solicitation, you are saying that the solicitation of friends and relatives to become potential prospects or clients is a deductible business expense if you talk business at any time during an evening with them. That is the advice you are giving the people, and you are saying that is the law?

Mr. **Fields**. That is the advice——

Mr. **Fowler**. Yes or no.

Mr. **Fields**. That is not the advice that I am giving.

Mr. **Fowler**. That is what you gave on the tape.

Mr. **Fields**. That is what I stated at that time to an audience of actively building distributors.

Mr. **Fowler**. Doesn't make any difference. The law applies to everybody whether or not they are actively building distributors or not. That law, that advice applies to every citizen taxpayer in the country. Is that the law that you are advising or is it not the law?

Mr. **Fields**. That is the law that I advised, yes.

Mr. **Fowler**. And you are saying you think that is the law?

Mr. **Fields**. Yes, I do.

Mr. **Fowler**. Mr. Fields, on tape, and I quote,

> You know you are going to be visiting a relative in Florida. So you send them a letter out to tell them that you are coming there and talk to them about a fantastic business with super tax benefits, and ask for them to send you a letter back confirming the date.

You are saying on that tape, are you not, that that would make that a proper deductible business trip. Is that the law?

Mr. **Fields**. Only if there was substantial business activity.

Mr. **Fowler**. That is not what you said. It is not the law, is it, Mr. Fields?

Mr. **Fields**. I have already admitted that that tape is subject to misinterpretations.

Mr. **Fowler**. No; that isn't what you admitted to. That is what is disturbing me. What you admitted to, trying to gain a little sympathy, was nervousness and immaturity and naivete in speaking before an audience. We all are nervous and naive when we speak before an audience, too. But there is nothing in your statement that admits that you were giving false tax advice. I think it is obvious that you were giving false tax advice. Do you admit to that?

Mr. **Fields**. No; that was not false tax advice.

Mr. **Fowler**. If I am going to Florida to see my relative and I want to go down and watch baseball spring training, and I write a letter to them and say, "Oh, I also have a wonderful business that I want to talk to you about, if you will just send a letter back to me confirming that I am coming down there," you advised that that would be a legitimate deductible business trip; meals and plane tickets and all the ordinary and necessary deductions. Is that wrong? Is that the law? Is that the law, Mr. Fields?

Mr. **Fields**. No; that is not the law.

Mr. **Fowler**. That is what you told them, was it not? On that tape of March 1980?

Mr. **Fields**. Those facts have been embellished. That 1980 seminar——

Mr. **Fowler**. Wait a minute. No facts to be embellished. That is what you advised them in March 1980, that we just heard on that tape that you said you were speaking. Isn't that correct?

Mr. **Fields**. Again, that advice was given to a group of distributors who were actively building, and the assumption could be made that if they went there, they would have continued actively building their business in the area that they were traveling to.

Mr. **Fowler**. Mr. Fields, I could go on through your foreign travel comments, your ski house, ski condominiums, your beachhouse. But it is obvious that you were giving false tax information. Perfectly and plainly obvious. By a man who knows better, who had gained that in a public occupation paid for by the taxpayers, selling your experience as an IRS agent to become an expert.

And I think it is just totally reprehensible. For you to answer me or any member of this committee about what your assumptions are, assuming this and that and that and that from any member of the audience simply does not hold water.

That is all I have, Mr. Chairman.

Chairman **Stark**. Mr. Martin.

Mr. **Martin**. Thank you, Mr. Chairman.

I have, as everyone here has done, followed the questioning of my colleague and the witness, Mr. Fields, regarding the presentation of what might be called false tax information. Mr. Chairman, the only thing that concerns me at all about that is that on the copy of the transcript which was presented to us, there is, at the conclusion of one sentence regarding visiting the relative in Florida and the fantastic business with super tax benefits, and getting a letter back confirming the date, three stars which corresponded to a pause on the tape that was played to us.

My only concern there is if there was something else in the tape at that point that was omitted because it didn't appear to be relevant but which might or might not have something to say about the quoted material.

Could I make a request, if a nonmember of the subcommittee can make a unanimous consent request, that we include, in the part that will be in the record at least, the transcript of the entire segment?

Chairman **Stark**. If the gentleman will yield——

Mr. **Martin**. Each of the passages——

Chairman **Stark**. That is part of the record. We have a copy for you here of the entire transcript of the tape. Those segments that you heard on the shorter tape were indeed taken out of context. But I think you can see in the full—they were merely illustrative.

We have both transcripts which will be made part of the record.

Mr. **Martin**. So you can look at the entire transcript.

Chairman **Stark**. Indeed.

Without objection the entire transcripts will be part of the record and are available now.

[The information follows:]

EXCERPTS FROM TAX TAPE

I'm talking about the areas where you're already spending money expenses you already have and converting those personal expenses into business tax deductions. How are we able to do this? Well simply since we are each independent businessmen or women we can deduct expenses for promoting or developing our business.

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Taking that one step further, let's say someone buys a Seville and your talking about a $24,000 car. Now your talking about $2,400 tax credit just for buying that car. Nice way to get the government to make your downpayment. You know through this business you can literally convert your car to 100% business use.

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Since all of your friends and relatives are either potential prospects or clients or currently prospects or clients. Almost any time you go out with a friend or relative you can convert it to a business expense if you'll talk business during part of the evening.

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How many people do you give birthday gifts to? How many people do you give Christmas gift, or Hanukkah gifts, wedding gifts, baby showers? If you give them something that you purchase through this business—and representing over 350 manufacturers that gives you a lot of items to choose from—if you give them something from this business and you want them to be clients later (otherwise you wouldn't have given it from your business, right?) So that is right, just keep that attitude.—If you give them something from this business then that is a business gift and you can deduct $25.00 of it.

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You know you are going to be visiting a relative in Florida so you send a letter out to them telling them your coming there to talk to them about a fantastic business with super tax benefits and ask for them to send you a letter back confirming the date.

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Now on foreign travel you first have to establish business intent. Now it goes the same way by sending out letters and send them out ahead of time to anyone you know there. Send out letters to our corporate headquarters asking if there is going to be any functions taking place during the time you are going to be there.

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All you have to do is establish your business whether at your other beach house or ski condominum or the boat is moored there that is all you have to do. Then anytime you go up there to conduct your business all of your expenses are going to be deductible. Your food, eating out, cleaning, the upkeep on that property, depreciation (like you got on your car), the depreciation on your furnishings, investment credit on the furnishings of that beach house or that boat or that condominum.

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Now even a guest bedroom so long as any time a guest sleeps there you show them the business before they go home then that would be business purpose and you can take that room.

Telephone—What we recommend is that you get a separate telephone for your business and take all your toll calls on that phone. If through your business you purchase a television or a microwave oven or a vacuum cleaner or clothes or any of the items we manufacture ourselves and you use that item as a sample in your business then you may be able to take either a partial or a full deduction for those items.

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Now I'm going to show you another way you can save $4,000, $5,000, $6,000 in just the one area. This is the area of income transfer. There is a lot of things that children in this business can do to help you in this business and you pay them a salary. Now when you pay them a salary that is a tax deduction to you and if it is less than that $3,800 the children pay no tax on it.

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If you can show that your bringing more people into your business that you are establishing more clients. If you are building your business, you can go on indefinitely taking a tax loss against other income because of the business intent.

TRANSCRIPT OF ALAN FIELDS TAX TAPE

This afternoon I am going to be talking with you about tax benefits. There have been a lot of misconceptions in this business concerning the tax benefits and there have been both accounts who we know well people to take the deductions that they were legally entitled to, and on the other hand there are those accounts who maybe go a little overboard and take things which they are not legally entitled to. I just thought that it is about time that a former IRS agent set the record straight. During almost 6 years with Internal Revenue Service I literally audited thousands of tax returns and I cannot recall ever seeing even one other business that had as great a tax benefit as this business does. What I'm going to do is cover some of the areas that can save you as much as hundreds or thousands of dollars in tax benefits each year and even though you may not be able to take advantage of each of these areas I want you to think about those people that you know who can take advantage of them. I've heard people say that they were told not to take the deductions that they were entitled to just because they would be audited. That is ridiculous!

First, just because you have a business on your tax return is not going to cause you to be audited. Only 2½ percent of all business tax returns are audited. Most returns are selected by computer and a numerical scoring system and IRS in Fresno runs it through the computer and they select the returns that have the largest number of points. At this time we have over 30 Internal Revenue agent employees that are involved with us in our business and combined experience is probably in excess of 150 years and yet after talking with those people the grand total of all returns that they had audited that involved this business was only 10. I personally only saw one return involving this business in the entire six years that I was with IRS.

Second, just because you are audited does not mean you are going to be paying back any money, going to jail, doesn't mean anything like that. In fact, the one return that I audited I accepted it as it was filed. There was no change at all. All of the deductions that they were taking were legitimate business deductions. There was one other return that was audited that I am aware of and in that case what actually happened was the taxpayer received an additional refund of over $600 because their account had not even taken all of the deductions that they were entitled to.

Before getting into specific expenses let me just go into a couple of the reasons why we even have to do this, why this is even necessary. Go back a couple of years ago and at that time a family with an income of $15,000 all they would have been paying in state and federal income tax would be $1,600, now because of inflation, cost of living increases, etc., that same family earning about $35,000 their tax would be $8,500 between the federal and state. That is 130 percent increase in income but a 430 percent increase in taxes. It is because of this increase in the percentage of taxes that people are paying that they started looking around for ways to shelter it because you take this family and $35,000 a year in taxable income they are paying on each additional dollar that they earn 54 percent to federal and state. That is the same thing as saying for each additional dollar that you earn you get 46¢ that you get to keep. That really is not very much. I don't like working for less than half of what I'm earning so when they tell you inflation went up 15 percent last year we are going to give you a 15 percent cost of living increase all you really have after taking into consideration the taxes is less than 7 percent which isn't very much at all.

When Congress set up the tax laws what they basically said was everything is taxable and nothing is deductible. Every tax law which fills volumes this thick all they are is exceptions to the basic rule and as inflation has pushed more and more taxpayers into those higher tax brackets they've had to look for ways to take advantage of those shelters, ways to take advantage of those exceptions to the tax laws. We talk about tax shelters and a lot of people think that is a bad word, but taking a tax shelter is only taking advantage of laws that are available to you and there is nothing dishonest or anything illegal about doing that. IRS will not penalize you for evading taxes through legitimate tax shelters—only if you are avoiding taxes. Now some of the areas that people got involved in are oil and gas leases, mining interests, rental properties, film productions, television rights. Now these originally were legitimate tax shelters but over the last few years as more and more companies went into the tax shelter business what happened was that you started seeing tax shelters where people had invested a lot of money and there was never any intent of making a profit on that. All they were supposed to do was to get tax benefits that were greater than what they had paid. So if someone invested $10,000 into one of those tax shelters they were taking tax deductions of $20,000 and that 54 percent as you can see they would get back in taxes more than what they had paid for the investment. What happened is that IRS caught on to that and the 1976 and 1978 Tax Reform Acts virtually knocked the wind out of many of the traditional tax shelters. In fact when I left IRS there were a number of partnerships under audit in the oil and gas leases especially. Some of those involved as many as a thousand to ten thousand partners in the southern California area and they all had one thing in common—IRS was disallowing all of their deductions. Here were sophisticated taxpayers many of them doctors, attorneys, accountants who have lost their investment because there was never any intention of making profit and at the same time they lost all the tax benefits that they thought they were going to get. So those types of tax shelters are just not the place to be right now. In fact, just last month the Commissioner of Internal Revenue Service released a note on announcement in which he said that the IRS was going to increase its audit activity in the abuse of tax shelter areas and when asked what abusive tax shelters were it was those items that I mentioned above. Now real estate itself is not necessarily an abusive tax shelter but many people are finding it harder to get tax sheltering effects through real estate. The idea was you put in a small amount of money and get large tax write-offs and in that way we cover the investment that you put and in over a long period of time make a profit. But with mortgage rates going up to 16½ percent and banks requiring 30 or more percent down we lost that benefit. So what did that leave? The only tax shelter left for the average person was having a business. The 1976 and 1978 Tax Reform Acts also limited a lot of tax deductions that self-employed people were taking. However, each time IRS restricted or eliminated an area for self-employed people they also provided rules that if you meet those rules you would still be able to take the deductions. Now this business was started over 20 years ago and I know that when they founded this company they weren't interested in establishing it just for the tax benefits and I know that there is no way that they could have known that the tax benefits would be 20 years later but just because of the very nature of the program that they put together those of us in this business today can meet those new rules and take deductions that many other businesses have lost. Many accounts won't take the time to sit down and take a look at why this business meets those new rules. You have to understand that most accounts are doing 500 or 600 or 1,000 tax returns in just a 3 month time and if they have one or two clients involved in this business they just can't justify taking the time to research it in order to get the information that they need. I've had a number of people come to me and say that their accountant told them it wasn't even worth putting on the tax return. That just isn't so! In the tax returns that we have done so far this year the smallest tax savings is a direct result of this business was over $800 and the largest was in excess of $3,000 in tax savings and that was before taking into consideration some of the areas that I am going to go over with you this afternoon. In fact, towards the end I am going to go into one area that will alone save you as much as $4,000, $6,000 or $8,000 a year in federal and state income tax. I just don't know anyone who can say that it isn't worth getting $800 to $3,000 in your pocket instead of the Governments.

The necessary and ordinary business expenses that you incur are deductible things like accounting, bookkeeping, bank charges, printing, stationery, postage but I'm not going to go into those types of expenses. What you can do is call your local IRS office and request a copy of the tax guide for small businesses and you might as well request it cause you have already paid for it.

Now I'm going to go into the areas of expenses that are different. I'm talking about the areas where you're already spending money, expenses you already have and converting those personal expenses into business tax deductions. How are we able to do this? Simply, since we are each independent businessmen or women we can deduct expenses for promoting or developing our business. Since we operate out of our homes many of the expenses we are already incurring and we have already paid for. For example, how many of you out there drive to work? Normally, the expense of driving back and forth to work is a personal expense; it's called commuting. It is not deductible. You put that $1.25 a gallon out of your pocket, you pay for your car, you pay for the repairs and you don't get anything back. In fact this year IRS even eliminated the gas tax deduction on your itemized deductions so you even lost that. You are not getting anything at all for commuting expenses. IRS has always maintained that if you have a minor business in your home and you had a major business someplace else that the cost of travelling between the two was still commuting expense. There have been recent court decisions in which IRS lost and what those tax decisions said was that if someone is operating a second business in their home the fact that one is producing more income that the other is not the determining factor in whether that person has a principal place of business as his home. The Tax Court says that if you are operating a separate business from what you are doing otherwise and you operate that out of your home that you can have two principal places of business. Now by having two principal places of business your mileage between the two becomes deductible. The only thing is you have to be doing something in that home but again the nature of this business can be listening to a cassette tape for training, you could look at one piece of paper and check it for accuracy, make a phone call to somebody you know on the east coast. Anything that you do in the business before you leave for work in the morning if you document that in your calendar then your mileage to work becomes tax deductible. The same thing going home. If you do something in your home after returning from work so long as you document it whatever it is, doesn't say that you have to be doing a lot just doing something, than your mileage home is deductible also. Now that mileage can add up to a lot.

There is two ways of deducting your mileage. First, the IRS allows you to take 18½ cents per mile for business mileage or your actual expenses. Now with the 18½ cents you can also take parking and DMV fees. Now take as an example somebody who is driving 20 miles a day each way to work which isn't very far most people drive that much or further. In that case, that person would have after taking the total mileage of 18½ cents they have over a $2,000 tax deduction and at 54 percent what I'm going to do is use that $35,000 a year income through the program that would be $1,080 in tax savings. How would you like the government to pay you $1,000 for driving back and forth to work. Not bad! Make up for that high cost of gasoline. If somebody is driving further I know before I went full time in the business I was driving over 100 miles a day and we would be talking about several thousand $3,000 or $4,000 in tax savings for someone in the $35,000 bracket.

On actual expenses what you can take is your depreciation, or if you are leasing the car then you would be taking your lease payments, your gas, oil, repairs, maintenance, license fees, automobile club, auto insurance, parking and any other maintenance or repair item including cleaning, waxing on your automobile. For most people with compact cars or cars that are older than a year or two years you are generally going to be better off by taking the 18½ cents a mile. However, if you have a car that gets poor gas mileage or it's a brand new car then you may want to take actual expenses. There is one other area that you get by taking actual expenses. When you depreciate your car what you're doing is spreading that over a five, six or seven year period of time. So if you spent $14,000 for the car and you spread it over seven years that would be $2,000 a year in deductions for depreciation. As you can see that would again be $1,000 tax savings before taking the gas, oil and all those items. Also in the first year that you purchase the car even if you purchase it on the last day of the year you get a bonus depreciation of 20 percent which in this example would be $2,800 in depreciation. Again, we're talking about $1,000 or more in tax savings. This is a bonus plus the $1,000 in tax savings for the regular depreciation or over $2,000 in tax savings just because you bought a car that was $14,000.

Now in addition to the actual expenses, there is another area that you get when you purchase an automobile and this doesn't matter whether you are taking the mileage rate or the actual expenses and that is investment credit. I don't know why but so many accounts seem to miss investment credit. The way this works is any time you buy a capital asset for your business and a car is a capital asset, furniture for your office is a capital asset, typewriters, adding machines, anything that lasts more than one year that is used in your business is a capital asset. And with the capital asset you get investment credit and investment credit is equal to 10 percent of the purchase price of the item and again it's even if you can buy it on the last day of the year. If you buy that car and start using it for business on December 31st you can get the investment credit. Now if you are going to use your car for less than 7 years the credit gets reduced but you still will get some credit. To give an example, if you buy a $9,000 car at 10 percent would be a $900 credit. Nine hundred dollars in your pocket. Taking that one step further, let's say someone buys a Seville and your talking about a $24,000 car then you're talking about $2,400 tax credit just for buying that car. Nice way to get the government to make your down payment. Through this business you can literally convert your car to 100 percent business use. Almost anything you do in this business is related to prospecting or dealing with people already in the business, potential clients, potential associates in your business, anything you do is business related and if all you have to do is document that in your calendar and keep track of what you are doing almost anything can be business. Let's say you don't want to get up in the morning and do something, all you have to do is drive to the bank first before you go to work, make your deposit through their instant deposit window and then the mileage from the bank to work would be deductible. It is better just to put something down on your calendar each morning then you're covered.

Since the family becomes an integral part of your business. Since your spouse becomes an equal partner we are really talking about two cars because your spouses expenses can be 100 percent business also, if you'll document it. This has been upheld in the Tax Court. Similar cases have gone to the Tax Courts and it has been upheld. Even IRS will allow 80 or 90 percent business use without documentation in this business just on oral testimony, but it is best to document it and then you'll get it all. So you can see that even just the automobile alone can provide many thousands of dollars in tax savings. You may not have a car or you might drive short distances, but just think about those people that you know who drive large distances and are good prospects for your business.

The second area I want to go into is entertainment expense. This is another area where you can get substantial tax deductions. The law says that you can deduct entertainment expenses in maintaining or promoting your business. This includes entertaining current or potential business clients or associates. This could be at your house, your boat, beach house, ski condominium or restaurant. There is no limitation as to where it is going to be so long as business is either discussed before or after and prospecting someone is considered conducting business. So it is very easy to show that you were doing something that was business related. Since all of your friends and relatives are either potential prospects or clients or currently prospects or clients almost anytime you go out with a friend or relative you can convert it to a business expense if you'll talk business during part of the evening. The IRS doesn't say the entire evening has to be business—only that business take place before or after. And there is another area which makes it even easier. IRS says that quiet business meals are deductible. A quiet business meal does not need to have business before or after. What a quiet meal is is when you sit down with someone over lunch or dinner and you say—"Tell me, are you happy doing what you're doing?" "Are you looking for something else?" That is having a quiet business meal and you can take the deduction for that meal including your own expenses. These are real taxes! Believe me. We got 30 revenue agents in the organization. That can add up to quite a substantial tax deduction. One thing that you have to do though is that you have to document what you're doing. Now what I suggest is that in your calendar take a corner in each page or each day and make sure that you get a calendar that is big enough so that you have room and you have to put why. You have to tell what the business purpose is and that can be very simply your prospecting someone or your doing a follow-up whatever it might be you put that down. You have to say where it is and that is very simple it is just where you are. You have to say who you're entertaining and that can be John Smith, my cousin, whoever it is you put down who you are entertaining. You have to explain when and when is simple because if you use your calendar it is already in there and the last one is how much and how much is just how much you spend. If is less than $25.00 all you have to do is write down the amount in your calendar. If it is over $25.00 you need the receipt also, but if you keep all your receipts it is better if you ever do get audited because the more stuff you go in with the less likely the auditor is going to look at it. It is true. It is called the bigger shoe box theory. So remember these five areas and the way Bob Schmitt remembers it is he calls it the five w's but since he is a diamond I'm not going to correct him.

In doing the entertaining there is another area that is a little bit different and that's called entertainment facilities. Now IRS really cracked down on the entertainment facility area and it has things like boats, yachts, beach houses, ski condominiums, social, fraternal and athletic or country clubs but again as in the other cases they always set up rules that allow you to least get part of the deduction. I am going to show you a way in a little while that you can get even more but on the entertainment facility aspect that if you can show that it was used more than 50 percent for business, and this is pretty easy to do because in this business again because of the nature of being able to deal with your family and friends you can show that anyone you take with you to one of these places is business related just document it in your calendar. You can take your family up—just talk to them about the business while they're up there that's all you have to do. If you can show that more than 50 percent is business related than you can still deduct the operating expenses of that beach house, ski condominium, boat or airplane and you can still deduct the dues for a club whether it's a country club or social club fraternal or athletic whatever it might be. You are going to have to show that it was used primarily for business more than 50 percent so just document every day, document how it was business related in your calendar.

Everyone around is a prospect for your business. You can show a very high percentage of business use and be able to take a large tax deduction. Who do you know who has a beach house? Who do you know who has a ski condominium? Who do you know who belongs to a country club? All those people are prospects for your business. Another area is gifts. I like this one. You will too and I'll show you why. The IRS says that you can give business gifts to promote or develop your business and they also say that the people who you are giving the gifts to can be either current or prospective clients or business associates fits in there also. This means your family, friends, your relatives, anybody. You can give gifts up to $25.00 a year per person. You can give more but that is all you can deduct. Think about it. How many people do you give birthday gifts to? How many people do you give Christmas gifts or Hanukkah gift, wedding gifts or baby showers? If you give them something that you purchased through this business and representing over 350 manufacturers that gives you a lot of items to choose from. If you give them something from this business, you want them to be clients later otherwise you would not have given it from your business, right? If you give them something from this business that is a business gift and you can deduct $25.00 of it. Give out 10 Christmas gifts $250.00 tax deduction—birthdays during the year—whatever it might be because it is not limited to the number of gifts it is only limited to $25.00 per person but there is no limit to the number of persons. That can be very substantial and what a way to convert expenses you already have into tax benefits. People will be wondering why you give them better gifts than you did before. Tell them and bring them into the business.

Now since this business is open to you throughout the country and virtually throughout the world we get into another area which is travel. The IRS says that if you go away from home travelling to build or promote your business then you are entitled to the expenses. All you have to do is show business intent. Business intent meaning that the main purpose of that trip was to conduct business but it is my feeling that if you go to a wedding in New York and there is going to be 200 people there that those 200 prospects certainly were a lot more important than going to the wedding, right? All you have to do is put into your calendar and say that you went to this wedding for all these prospects and while you're there get their business cards, write it down and you can take that trip. One of the things that we do is send out business correspondence. You know that you are going to be visiting a relative in Florida so you send out letter to them telling them you are coming there to talk to them about a fantastic business with super tax benefits and ask for them to send you a letter back confirming the date. What you have done is establish business intent. Goes along with the bigger shoe box theory. If a revenue agent sees that you got in that much trouble they'll slide over that and go on to the next area. So you can get it through fairly easily.

It's a little bit more difficult when you're talking about foreign travel. Let me just back track for a second. On travel locally in the United States your family goes with you and if your wife is the one who is most active in the business it is the husband that goes. Your spouse is an active partner. Now most business they cannot deduct their spouse travelling with them. Well, they can deduct it but if they get audited IRS is going to throw it out but since the spouse is an active partner in this business you can show the business purpose and deduct all the expenses for your spouse. Now on foreign travel you first have to establish business intent. It goes the same way—send out letters ahead of time to anyone you know there, send out letters to our corporate headquarters asking if there is going to be any functions taking place during the time that you are going to be there. Set up your business intent because if you set up the business intent IRS can't do anything to take that deduction away from you if you set it up properly to begin with. Now IRS says that if you can show business intent and it's less than 7 days, which most people don't travel to foreign places less than 7 days but Hawaii is considered a foreign travel so you might go to Hawaii for less than a week, and you can show business intent then you can deduct all the expenses i.e., travel, lodging, all of your meals while you are there even if you don't do business every day. And if you want to stay more than 7 days the IRS says that if it is more than 7 days then 75 percent of the time or more must be used for business. If you go and do something regarding business for 2 hours in the morning that day is considered a business day. If you go Hawaii on a moving up seminar and you go to the first couple of hours in the morning to the seminar that's considered a business day. Any day in which you conduct at least a portion of the day business is considered a business day. Also, weekends are counted as a business day if you conduct business the day before and the day after the weekend, which is kind of an easy way to go. Also, travel days—the days that you're traveling from the United States to that other country or to Hawaii the two days combined count as one business day not as a personal day. You can show business days very easily. To give an example on how few days you can really put in doing business and be able to deduct your business trip. Let's say you leave for Japan on Wednesday that equals one-half of a business day and you get there and Thursday you relax and have a personal day and then on Friday you conduct business. Let's say you take a tour of our corporate headquarters. Not too difficult, right? You get a business day. That makes Saturday and Sunday equal to business days no matter what you're doing and you still have business days. Monday, you actually do business—show somebody the opportunity, take somebody to a function being put on by our corporate headquarters over there, whatever it might be—you do something with the business that day so you have Monday as a business day. Tuesday, you do a business day also. Again, just something simple a couple of hours that day and then Wednesday, you do whatever you want as a personal day, and Thursday, you're going back home it's a travelling day so it's one-half of a business day. Now what you've actually done here is you've worked business three days. You worked business Friday, Monday and Tuesday. You were actually gone for 9 days but since these days count half days IRS says okay you have eight days that you were gone and you have six days that are counted as business even though you only actually only worked business for 3 days and had 6 days in which you were doing other things and only two of those days count as personal days. So you have 75 percent business time and only 25 percent personal even though in actuality you only had 30 percent of your time with business time and IRS says that if 75 percent of your time is business and all you have to do is set it up so that you get the weekends in there and put a workday on either side, IRS says that if you have 75 percent or more is business then you can deduct your transportation, both ways plus you can deduct expenses on any day that is considered business. So the only expenses you would not be able to deduct would be this Thursday and Wednesday, the two personal days. You would be able to deduct all the expenses of sightseeing on Saturday and Sunday and all the expenses on all the other business days even though you only spent a couple of days doing business. So keep that in mind if you are going to do any foreign travel because that way you can establish that it was business and be able to take that write-off. Foreign travel can get to be very expensive and it's kind of fun to have the IRS pay for half of your trip. Is there anybody who doesn't want IRS to pay for half of their trip? I didn't think so.

Going along with travel there is an area that's called being away from your tax home. The IRS has always said that when you're away from your tax home all your expenses are deductible which is what we've done in the travel expenses. However, IRS defines your tax home as being the principle area in which you live, conduct business, maintain checking account, savings account, other investments so that would be normally the place where you live during the week. If you leave that tax home to conduct business, you're entitled to the expenses. What that means is that—I told you I would get to this—if you have a beach house or ski condominium or a boat you can sleep on or a plane with sleeping areas on it and you go away from home overnight to conduct business you can deduct those expenses. All you have to do is establish you're business whether at your beach house or ski condominium or the boat is more. So if you have a beach house in Malibu, you just have to bring some people into your business in that area or establish some clients. If you have a condominium in Mamouth, all you have to do is sponsor someone into your business who is in Mamouth or get a commercial account up there that's all you have to do then anytime you go up there to conduct your business all of your expenses are going to be deductible. Your food, eating out, cleaning, the upkeep on that property, depreciation on your furnishings, investment credit on the furnishings of that beach house or that boat or that condominium, especially if you show that every time that you go up there through your calendar show that you were doing business. And make sure that you get a calendar that you can open up because when January and February are over you want to take January and February's pages out because if you went to Japan in January and document all this stuff you don't want to lose that calendar in June and then not have it.

IRS bought this for a long time and there are a number of court cases on being away from the tax home and it has been won time and time again by the taxpayer so there is no problem in doing it, but it is not just prospecting in that case you have to actually show that you're operating your business. So all you have to do again is either sponsor someone to bring them into your business or establish your commercial account or even a home account and you can take those expenses.

Let me get a little closer to home. Many occupations use to be able to take a home office deduction and in the 1976 and 1978 Tax Reform Tax Acts, mainly the 1976 they virtually eliminated the home office deduction. All of those types of occupations i.e., teachers, doctors, attorneys, anyone who did any work in their home besides their other office those people were taking a home office deduction. Well, IRS eliminated that but as in the other cases they set up rules that would allow you to still be able to take those deductions. What they said is that the portion of the home that you use as an office must be used exclusively and on a regular basis as a place for meeting, or dealing with clients, customers or prospective clients or customers. Since we work out of our home and because of the type of work that we do we meet that requirement because regularly can be one day a week so long as it's being used only for that purpose. Now even a guest bedroom, so long as anytime a guest sleeps there you show them the business before they go home then that was a business purpose and you can take that room. You also get any areas used for storage. So it would be storage of inventory, and if you are writing your automobile off 100 percent then the area for storage of your automobile counts also. So that can be a lot of area. Some of the things that you get in office in the home—you get depreciation on your home or if you're renting it would be the rent, utilities, repairs, maintenance, landscaping, maid, painting, pest control, if your in condominium than the homeowner's association fees, any of the expenses in operating and maintaining or repairing that home are added together. Let me give you an example on how it works. Let's take a $100,000 house. You should watch this because many of the accountants that you'll be going to are going to tell you that you can't get office in the home deductions. You're definitely entitled to it and this is the way to compute it. Now what you do is you have to depreciate your home over a certain period of time. Normally we use 30 years so that would be $3,333 a year for depreciating your home, or if your renting it would just be the total rent payment for the year. Now let's say $2,000 in utilities, and maybe another $2,000 which included painting part of the house and some gardner and a maid that came in once a week or a total of $7,333 in expenses for operating and maintaining your home. Now we take the area used for business and let's say there is a combination of the storage area and the room being used for let's say 300 square feet—take the square footage of each area and then add it together—and say a total square footage for the house of 2,000 square feet which would give you 15 percent that would be business use. So what you would be able to deduct on your tax return would be 15 percent of that which comes out to about $1,100 and going back to our $35,000 a year example that would be $590 in tax savings. Now take that room that you're not using for anything else and convert it to a office and you get that extra tax savings an extra $590 almost $600 a year in tax savings. One of the ways to document the business use of your home is to get a guest book and have everyone who comes in sign that guest book—don't forget the television repairman is a prospect for your business, don't forget the plumber is a prospect for your business, whoever comes in there, the parents of your children's friends when they come over to pickup their children—have them sign that guest book so that you can establish the business use. You can also take any other area of your home—if you have a formal living area and it is never used for anything else, nobody ever goes into that room except when you put on business meetings, then you can even take your living room area the same way by taking the square footage. You have to be able to show—and IRS would look at that a little more closely because they find it hard to believe that you don't use your living room for anything else—and keep records in your diary and you can establish that.

On the telephone—what we recommend is that you get a separate telephone for your business and take all of your toll calls on that phone, all of your extended services on that phone and then deduct that phone 100 percent because if you call your aunt or your uncle, mother, cousin, they are prospects for your business just make sure you mention something when you're on the phone. A call doesn't have to be totally business all it has to be is business related and no one would expect you to just call up a relative in New York and say—"You want to get in my business?" You're going to have some social talk first so you can't take your telephone expenses very easily as a business expense if you'll get a separate phone and then keep the one phone for personal use—get the lowest base rate that you can and keep the other phone strictly for business.

One area that is a little bit sticky, IRS frowns on it but you can take these deductions and if you were audited you should be able to get them through, is promotional items. Since we represent over 350 name brand manufacturers, as well as the products that we manufacture, there are a lot of items that you can use for yourself and you can get substantial tax benefits in the area of being a sample or promotional item. For example, if through your business you purchase a television or microwave oven, a vacuum cleaner, clothes or any of the items that we manufacture ourself and you use that item as a sample—"Hi John! Came over to see the Superbowl. I just want you to know if you ever want a television I can get it for you." That is a sample. Isn't that a sample? So long as you use it as a sample in your business then you may be able to take either a partial or a full deduction for those items. If it is something that lasts less than a year such as most of the items that we manufacture then you can take it the entire expense in that year if it was a promotional item. On the other hand if it is something that lasts more than a year, you have to depreciate it over the period of time that it is going to last. For example, take a videotape recorder—we have a videotape recorder in our catalogue right now—say $1,200 for a videotape recorder and let's say it lasts for three years that means that your depreciation or the tax deduction you could take would be $1,200 divided by 3 or $400 per year and back to our original example of 54 percent tax for the $35,000 income we would be talking about $216 a year in tax savings or a total tax savings of $648 which means you only paid $552 for that videotape recorder and the federal and state government paid the other $648. The same thing goes for the microwave ovens, vacuum cleaners or anything that would last more than a couple of years. That can be a great way of going. We have people who are interested in the business and say—Well, I can get that cheaper at Memco. Show them the tax benefits—I would like to see them buy that at Memco for $552—no way. Good point there from the front row. You also would get the investment tax credit on this, however, that since you are only doing it for three years you would get an investment tax credit on only ⅓ of that which would be the $400 times 10 percent or $40 tax credit in addition to everything else. So that actually brings your price to $512 instead of $552.

An important area in getting large tax deductions, if you remember in the beginning I said I was going to show you an area where you can save $4,000, $5,000 and $6,000 in just the one area is the area of income transfer. Through this business in the form of salary you can transfer legally to each of your children, minor children or fulltime students up to the age of 21, last year it was $3,300 but this year with the exemption it should be up to $3,800. So this year you should be able to transfer $3,800 in the form of salary to each of your children. The nature of this business allows you to have things that they can do. Even a three year old can stock shelves, a ten year old can do cleaning up, can start doing the paper work, a 14 year old can take care of all the paper work, answer the telephone. There is a lot of things that children in this business can do to help you in your business and you can pay them a salary. Now when you pay them a salary that is a tax deduction to you and if it is less than that $3,800 the children pay no tax on it and minor children working through their parents do not pay any employment tax. So the whole thing becomes tax free. Now you have to set this up properly, you are going to have time card, you are going to have to document what their doing in order to be taking it, but it is well worth it. Let's take for example, a family with $20,000 a year in income even they would save $1,300 in taxes by transfering that income to their children to one child. In our other example, the 54 percent it would be $2,250 that you would save in federal and state income taxs; two children would be $4,100; three children would be $6,150. That is a lot of tax savings. It's almost worth going out and having a couple of more kids—I guess. Well, maybe not! That is a lot of tax savings. Who do you know who is in a high income tax bracket who would like to be able to transfer money to their kids? You know, once you give that money to your kids it can be used for anything. They can pay their own private school tuition. They can buy their own clothes. They can do anything they want with it and you just had to transfer it to them to begin with but once you have done that your all set they can do whatever they want with it. Any divorced people out there? What a great way if your kids are with you on the weekend you put them on salary and you have them pay their own child support. I thought you'd like that one! Just remember if your going to do that, make sure that you sit down with an accountant and set it up properly, don't try to set it up after the fact do it in the beginning and you'll be able to take it because the law says that you can have anyone work for you that want. There is no law that says your children can't work for you. I rather hire my children than hire somebody off the street. I can trust them more—my son is 2½ years old and I can trust him more than anyone off the street. So don't be afraid to do that but just make sure you sit down with somebody and set it up properly to begin with and that's a good way to get high tax bracket people into the business.

One area that has been of concern and this will be the last area that I will go into to a lot of people is the IRS provision it's called Code section 183—activities not engaged in for a profit. What that code section says is that you must show a profit in two out of five years. There is one thing that most people forget though which says that unless you can show business intent and if you continue to build your business and if you can show that your bringing more people into your business and establishing more clients you can go on indefinitely taking a tax loss against other income because of the business intent. This business does over $1 billion a year. There is national advertising. The business is getting a lot of prestige. There are people generating large incomes so it is easy for you to show if you have to show it. It is very easy for you to show that you do have a business intent and that's all IRS is concerned with so don't be afraid to take those tax deductions and even if you were not allowed to take it against other income you can always take tax deductions against the income so you can continue to show a zero profit. All you do is you add another kid and pay him a salary. You can always write off against the income but don't worry about writing it off against other income. We're talking about a lot of taxes.

Now what I've done is just basically given you an overview and a lot of these areas do take documentation. It does take the requirements that you maintain good receipts, good accounting records in order to take them but what I wanted to do is that I want you to realize that there are many tax benefits that are available to you and to the prospects in the business. I want you to realize that there are people out there that have very high incomes who are very good prospects for this business because of the tax benefits. You know this truly is the greatest business in the world and it is only fitting that it should also have the greatest tax benefits.

Mr. MARTIN. Mr. Fields, you said about distribution of that tape, "Neither myself nor the corporation of which I am president has ever profited directly from the sales of that tape."

Do you know someone else who profited?

Mr. FIELDS. I have no idea. I do not know.

Mr. MARTIN. So you never contacted anyone to see if they would let you profit from the use of your tape?

Mr. FIELDS. No.

Mr. MARTIN. The tape of your remarks?

Mr. FIELDS. That is correct.

Mr. MARTIN. Did you contact anyone about ceasing to distribute your tape?

Mr. FIELDS. Yes, I spoke to a law firm, our corporate attorneys, in February of last year and was told that because we were unable to determine exactly who it originated from nor who was actually duplicating them at this time that there was nothing we could do to stop it.

Mr. MARTIN. So you don't even get a royalty fee for it?

Mr. FIELDS. No; I don't.

Mr. MARTIN. You say you have gone to great expense to counteract the tape and you talked at about 25 seminars. Were they free?

Mr. FIELDS. Most of those seminars were free, that is correct.

Mr. MARTIN. You refer to 25 you have personally given; then you say your associates have given 600 free tax workshops.

Mr. FIELDS. That is correct.

Mr. MARTIN. Some of the seminars you personally gave were free?

Mr. FIELDS. Most of them were.

Mr. MARTIN. Most of the 25 were free.

Mr. Fields, you say you published a newsletter. "I published a newsletter setting forth in frank and clear language the legitimate tax deductions an active direct sales person may claim, stressing the business intent." Then you put a quotation to try to clarify some of the previous misrepresentation or possible misrepresentation. You published it.

Did you mail it? Just so we will be sure what you are saying to us there. Did you mail out the newsletter?

Mr. FIELDS. Yes; we did.

Mr. MARTIN. How large a mailing list did you have for it when you sent it out?

Mr. FIELDS. In the neighborhood of 10,000.

Mr. MARTIN. In the neighborhood of 10,000. So you mailed to 10,000 subscribers or clients, or whatever, the information that you quote verbatim here?

Mr. FIELDS. The newsletters are mailed to anyone in the direct selling industry who requests it. We do not charge for them.

Mr. MARTIN. Thank you very much. Thank you, Mr. Chairman.

Chairman STARK. Mr. Fields, there were two items in your tape. I can, I guess, see a certain amount of exuberance, even you might say demagoguery, we are always accused of doing that in our profession. But I think it was your quote that even a 3-year-old can stock shelves which led several of us to earlier take exception to that.

Do you mean that literally, or are you suggesting that it is conceivable to have young children participate in a family business if they indeed do productive work?

Mr. FIELDS. Perhaps not as young as 3 years old; correct.

Chairman STARK. Another one I think comes dangerously close to being misadvice, but I don't know. You recommend getting a separate telephone for your business, and placing—this is the quote, "all your telephone calls on that business phone."

Now isn't there an extreme danger that somebody could illegally convert personal expenses or make personal calls on that business phone, and that that would be a clear violation of the law if they were deducting those toll calls?

Mr. FIELDS. That is correct. The intent of my comment was to include all business-related toll calls.

Chairman STARK. So if you had said all of your business related toll calls, OK. Wouldn't you agree that in the hands of either an unscrupulous promoter, or a naive businessperson, that there is a lot of room, as the Commissioner of Internal Revenue indicated before for people in general, without regard necessarily to direct sellers or any other profession or vocation, to be taking a lot more in the way of business deductions than they are entitled to, just as a general problem abroad in the land today?

Mr. FIELDS. Yes.

Chairman STARK. That costs all of us who legitimately try to pay our tax. If we could collect all that was honestly due, everybody could pay less. Is that correct?

Mr. FIELDS. That is correct.

Chairman STARK. Let's try the other side of this for a minute. If we were to try to establish some rules, play the devil's advocate for me and let's say we passed a rule that said, well, we will give something away to start with. The carrot is that the first $300 or $400 of gross receipts from any direct seller would just be entirely exempt from tax. We will assume it costs you $300 or $400 to generate $300 or $400 in sales. So to save your former colleagues and us a lot of rules, we will just pick a figure, say, first 300 bucks you report, but we will assume it is all expense and that is the cost of getting started. But that unless you get to $300 or $1,000 or some other level of sales, you can't deduct any expense for this secondary income.

How about a law like that? Would that cut down, do you think, on a lot of abusive deductions?

Mr. FIELDS. Could you repeat the question?

Chairman STARK. The question, to rephrase or repeat it is this. If I am right and there is some abuse by people taking excessive deductions, and using direct selling as just a way to take a lot of deductions, that is, the people you said shouldn't have your tape, people who were using it to promote recruiting rather than to promote true sellers. What if we just said that the first couple of hundred dollars would not be included in income? This would protect the low income person who gets in, attempts to do direct selling but cancels out because they don't make a go of it, just take a figure, $300, $500, $1,000. I don't care what level it is but some level of gross sales and say, unless you achieve that level you don't have to report any income or any deductions.

We will just assume that in selling the first modest amount you have used up enough expenses in going to learn about it, and cars and everything else. So we will say, you just don't report that.

On the other hand, unless you achieve a certain level of gross sales you can't deduct any expenses. Wouldn't that cut out a lot of abuse, a rule like that?

Mr. FIELDS. That is possible, but it might also cause a situation where the people who are actually showing true business intent and actively building a business who may not be growing as fast as somebody else might then have their deductions eliminated which would be legitimate deductions.

Chairman STARK. Some years ago we found, I believe, that a lot of people were really converting personal living expenses to so-called farm expenses. They were living in the suburbs and farms were getting smaller and homes were getting bigger. And the Congress found that it ought to put restrictions on what we call hobby farms. You had to show some reasonable expectation of making a profit.

I think they used a 5-year time span. What if we then applied that same type of test to the people who you were talking to at your seminars? Would you think that would be a fair rule to apply?

Mr. FIELDS. I believe that already applies under the hobby loss provisions, Code section 183.

Chairman STARK. So it would be your feeling that the hobby loss provisions would apply. So if somebody were filing returns such as the ones this committee has seen today and they go 2 or 3 years with very minimal, $300 or $400 in sales, and very large, 10,000 or 15,000 dollars' worth of deductions, they would lose those?

Mr. FIELDS. It would be very unlikely if somebody went that long with that type of situation that they would be legitimately building a business.

Chairman STARK. OK.

Mr. Vander Jagt.

Mr. VANDER JAGT. No questions, Mr. Chairman.

Chairman STARK. Mr. Fields, I want to thank you for appearing here today. I would ask if you would for me, as a matter of curiosity, to appear in the record, or not, as you choose, if you would be good enough to send to me, and I would make available to the committee, copies of your tax newsletter, in general, and any other newsletters that have applied to advice for direct sellers. I would be personally interested in seeing those.

Mr. **Fields**. I would be glad to do that.

[The following was subsequently received:]

ALAN FIELDS & ASSOCIATES TAX NEWSLETTER

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THE HOME OFFICE DEDUCTION

by Bob Nelson

In Section 280A of the Internal Revenue Code there are some exceptions to the law which allow a deduction under certain circumstances: 1. for use of the personal residence in a taxpayer's business; 2. for storing products as inventory; 3. as rental property; 4. or in providing day care services.

In general terms, that portion of the home which is used exclusively and on a regular basis for any of these four areas qualifies for the deduction and an allocable percentage of all related expenses such as interest, taxes, repairs and maintenance, cleaning, utilities, insurance, depreciation and any other directly related costs may be taken as an office expense.

In this first of a series on the home office deduction, we are going to deal with the term exclusive use. What is exclusive use and how does it apply to your business? In the following months we will define "on a regular basis"; what affect home office has on the sale of a personal residence; what specific costs are deductible in allocating the deduction; how major improvements to the home are treated; and which of these expenses, if any, qualify for home office deduction.

Exclusive use as defined by the Internal Revenue Service means for no other purpose. Following are some examples of home office activity. We will see which of these are either allowable, or unallowable and the reasons why.

EXAMPLES:

1) Bob and Linda have converted a bedroom in their home to an office that they use for their business. They keep a desk, chair, files and other miscellaneous office equipment in the room. The furniture in the room is used for no other purpose.

The room is used exclusively for the business, therefore the area qualifies in computing the deduction.

2) Jerry and Joan store all their products in a section of the garage where other personal items are also stored such as the lawn mower, etc.

The area used to store the products can be allowed in computing home office deduction. This is an exception to the exclusive use rule

continued page 3

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TRAVEL TALK

by Peb Conrad

This is the introduction to a series of articles dealing with the varied aspects of travel. Business travel can provide many benefits in the way of converting what would normally be a personal non-deductible item for tax purposes into a partial, if not totally, deductible expense.

This series will detail how to document your expenses, how to set up and carry out your agenda to receive maximum tax benefits, plus specifics on domestic travel, foreign travel and convention travel requirements.

The first area to be covered is some travel definitions.

continued page 4

FREE TAX REVIEWS
1978 – 1979 – 1980

Are you sure that you and your distributors have received the maximum tax benefits from your business?

As a service to our business associates, we will, at no charge, review prior years' tax returns for you or your distributors.

If you, or any of the distributors in your group, feel that you did not get all of the tax benefits available from your business, call us for an appointment to have your tax return reviewed by one of our tax advisors.

There is no charge for this review. If, after the review, you would like us to correct your tax return, we will do so at our regular fee.

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EDITORIAL "TAX-SIDE" CHAT

I hope that you will enjoy the new format for our newsletter!

The main purpose of this newsletter is to keep you informed on how the various tax laws can affect you, your family and your business. We welcome your suggestions and comments for "Your Tax Newsletter".

All of our "reporters" have their own Direct Sales Businesses, are former I.R.S. Agents or Auditors, and are currently employed full time as Tax Advisors with Alan Fields and Associates.

We will on a regular basis be covering Tax Benefits, Record Keeping, Tax Planning, Changes in the Tax Laws and Answering your Questions.

I would like to take a moment and remind you about two of the free services that we have to offer you.

First is our Free Telephone Tax Counseling. If you call us any Tuesday or Thursday, between 9:00 A.M. and 5:00 P.M., we will be happy to discuss any tax matters or answer any tax questions for you on the phone. If all of our advisors are unavailable when you call, we will take your phone number and have one of them call you back. Not all questions can be answered over the phone, but we will try to answer your question whenever possible. To have your questions answered, call us at (213) 986-3405.

The second free service that I want to tell you about is our Tax Workshop Program. If you get a group of at least 15 distributors together, we will have one of our former I.R.S. agents or auditors give your group a one hour Tax Workshop at No Charge!! The workshop will cover Tax Benefits in your business, recordkeeping for I.R.S. as well as a Question and Answer session. We can schedule a workshop for you any Monday through Friday evening. Call our office for more information on this program.

At this time, we are only able to offer these free workshops in the Southern California area. However, we are currently planning to expand our Tax Preparation Offices as well as the Free Tax Workshop Program throughout California and other Western States.

It continues to be brought to our attention that there are still some distributors that promote their business as a Tax Shelter. I want to emphatically state, as I have done before on tapes and at seminars, that your business is not a Tax Shelter but a business with fantastic income potential. Because of this income potential, those distributors who are actively building their businesses will gain some very substantial Tax Benefits. Just remember that the best way to get tax benefits from your business is to keep sponsoring and retailing.

Alan Fields

LEASE OR BUY AN AUTO

by Bob Frome

During this tax season many of our clients have asked, "Are there better tax benefits to leasing a new car, as opposed to purchasing one outright?"

Well, there really is no clear cut answer to this question; many factors must be considered before concluding which would be the better way to go.

During the next few newsletters I will be answering the following questions in detail, and explaining how each relates to distributors.

1. What is an open end lease, and how does it differ from a closed end lease?

2. Am I still entitled to Investment Tax Credit if I lease?

3. How are my expenses to be computed if I lease?

4. How do I compute my expenses after exercising my lease option?

5. May I claim depreciation on my leased car?

6. How do I handle the sales tax paid on my leased car?

Since each particular situation is different, please don't hesitate to write or call our office; we will be happy to help you.

TAX AUDIT SERVICE

Our IRS Enrolled Agents are fully qualified and experienced to legally represent you on all IRS Tax Audits, and other inquiries. Be sure to call 213-986-3405 (outside Los Angeles, call collect) for further information.

HOME OFFICE (con't)

since the area is being used for storage of retail inventory.

3) Fred and Barbara, who use their autos 100% of the time for business, keep them stored in their garage.

The area used to store the business automobile would be used in computing the home office deduction, since the autos are used exclusively for the business.

4) John and Mary use their living room in their home 3 nights a week to show the plan. They keep an extensive guest book and have all individuals who come into their home sign it. The room is hardly used for any other purpose except John's stereo equipment is in the room and on occasion the family listens to music and just spends time enjoying being together.

The tax deduction for home office would not be allowable since the room was not used exclusively for the business. As long as there is some personal use of the area (e.g. the family listening to music together) then no home office deduction is allowed.

5) Steve has a separate guest bedroom that is used only for putting up people overnight who have seen the plan in his home.

The room meets the exclusive use test but the area must be a place of doing business. Steve is not in the motel business and therefore the use of this room is not directly related to his activities in the busines. It's not in the normal course of doing business.

6) Jerry and Jan rent an apartment and use the kitchen table to do all of their bookkeeping and all other work related to the business. Jan spends an average of 4 hours per day at the kitchen table exclusively doing business.

Even though the time that Jan spends at the table doing the business paper work is substantial, it's not exclusive use since they use the table for their daily meals.

7) Walter and Marjorie use the kitchen on a regular basis, preparing food for business luncheons and home meetings such as potlucks.

The kitchen area is not used exclusively for their business.

Remember that not only must the area meet the exclusive use test, but it must also be used on a regular basis as place of business to meet clients or customers in the normal course of doing business.

To summarize, the requirement of "EXCLUSIVE USE" of a specific portion of the home eliminates deductions for any room which is for both office and personal purposes. It also bars deductions where a portion of a room is set off for office use and the rest of the same room is used for personal purposes. A liberal interpretation of "exclusive use" of a "portion" might allow the deduction where the office portion of a room is separated by a screen divider, etc., from the rest of the room.

Would you like to have a **TAX WORKSHOP** at your next potluck. Call for appointment for this **FREE** sponsoring and motivating tool. If not a Direct Distributor, please have your Direct call to set up this great program for your group. Call (213) 986-3405 (call collect outside of 213 area code).

TAX AUDIT PROCEDURE

by Jack Closson

Now that the smoke is clearing and filing season is behind us for another year, I thought I would take the chance to explain a phenomenon which everyone hears about but no one understands–TAX AUDITS!

The trepidation that most people experience when they receive an envelope from the IRS is directly related to those two words. In order to alleviate some of these fears, I will try to lay to rest the old wives' tales and mystique surrounding the audit process.

I have broken this subject down into several articles. In this way, if you have any specific questions, you may call or write them into us, and we will answer the most frequents ones in subsequent newsletters.

The audit process is six distinct, yet overlapping, groups: 1) audit selection process, 2) preparing for the audit, 3) your rights and responsibilities, 4) weighing your options, 5) Audit recurrence, and 6) the whole picture or summation.

AUDIT SELECTION PROCESS

As your return is processed at the IRS Center where you filed your tax return, it is assigned a mathematical formula and all data on the return is converted to mathematical symbols.

continued page 4

CLIENT QUESTION AND ANSWER COLUMN

by Andrew Smith

Q. Now that I have business deductions, should I increase the number of exemptions I am claiming at work?

A. Some people are telling others to claim as many as 99. The Internal Revenue Service is checking into all W-4's (Employee's Withholding Allowance Certificate) with more than nine withholding exemptions claimed.

This does not mean that you should claim nine withholding exemptions when you are only entitled to four. You should claim exactly what you are entitled to per the W-4 form. If you have a loss from your business, then you are entitled to more than the normal amount of withholding exemptions. You may claim 1 exemption for every person in your family and 1 exemption for every $1000 of business loss.

In the past there was a Form W4-E, but it has been incorporated onto the Form W-4. All this says is that if you had no tax liability last year and expect to have none in the current year, then you are exempt from Federal income tax withholding.

Be safe and claim what you are allowed, and this will avoid filing a fraudulent W-4 statement. If you have any questions regarding this matter, please give us a call.

AUDITS (con't)

The score or answer which results from this computation is stored by formula number for future reference. This is known as the "discriminant function" process (DIF) and has led many people to believe that by omitting or adding certain items to a return, you can beat the system.

A new system known as "total positive income" (TPI) is being instituted by IRS. This process only notes positive income items and does not recognize losses in determining DIF scores. The idea is to generate more audits among those people with large salaries or net profits who have found tax shelters to reduce their taxable income.

After all tax returns are processed, a computer generates the selection of returns to be reviewed for audit potential by DIF score. All tax returns having certain scores within a wide range of scores are selected for each formula used to be reviewed. Most people are never aware of whether or not their return has been reviewed until it gets much further in the selection process.

Starting with our next issue, we will delve into these other areas to try to better inform you about audit procedures.

TRAVEL (con't)

1) "Travel" – away from home overnight or at least long enough to require rest and sleep. Example – A distributor who lives in Los Angeles has an 8 A.M. appointment in San Diego. To make the appointment the distributor gets up at 5 AM. The day's agenda also includes lunch with their sponsor and an evening pot luck dinner at one of their downline distributor's home. The anticipated arrival back in Los Angeles will be 11 PM. In order to meet the long day's schedule, the distributor decides to rent a room at a motel (or a friend's house) to take a nap, freshen-up and shower. This example would constitute the rest and sleep requirement of the definition for "Travel" and all meals and other expenses incurred would be deductible. The "overnight" requirement of the definition would be that the distributor did not take a nap but decided to stay in San Diego at the end of the day and return to Los Angeles the following morning;
2) "Travel Expenses" – ordinary and necessary expenditures you had while traveling for your job, profession or business. You must have verification and/or documentation for these expenditures;
3) "Domestic or United States" – includes all 50 states and the District of Columbia EXCEPT for Conventions, "Domestic" would include U.S. possessions, Puerto Rico and the Trust Territories of the Pacific;
4) "Foreign" – includes everything outside of the 50 states and the District of Columbia.

These definitions will give you greater understanding of future travel articles.

Alan Fields & Associates maintains a full time office in Sherman Oaks (213-986-3405-outside 213 call collect) to aid you in all aspects of tax preparation, tax reviews, professional representation at audits, bookkeeping, and a host of other financially related activities. Our staff consists of active distributors who are former Internal Revenue Service agents and auditors. This past tax season we operated satellite offices in Ventura, Long Beach, Palmdale, Redlands, Sacramento, San Diego, San Francisco and Fresno. We are now planning to expand our office locations throughout California and other Western States. We certainly look forward to being of service to you.

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TAX AUDIT PROCEDURE

by Jack Closson

In last month's issue, I outlined the six audit process groups and discussed how a tax return is selected for review by the computer at the Internal Revenue Service Center.

Once the computer selects a tax return, it is sent to an Internal Revenue Service Classification group. This group will decide if the tax return is to be assigned to a correspondence or audit group, or to be taken out of the audit stream (surveyed).

If the return is assigned to a correspondence section, only 3 or 4 areas will be questioned, at most. These will be areas that can be simply decided without the taxpayer's presence and normally include interest, taxes, contributions, medical and some micellaneous deductions. More complex audits are assigned to field and office audit groups.

Before the tax return goes to either of these areas for audit, it must have the issues classified, in most cases. This means a tax technician will look over the return and select various areas on the tax return for the auditor or agent to question and verify.

After the tax return has been classified and assigned to a particular division, the taxpayer will receive a letter from that division explaining the audit process in general and a form requesting the records for the areas selected for audit.

It is advisable to remember that simply because your tax return has been selected for audit does not mean that there is an error or an illegality has been noticed. We at Alan Fields and Associates have found that if you have all the necessary records to answer the auditor's questions, your tax return will be accepted as filed.

An item most people are not aware of is that an audit can be transferred for the convenience of the taxpayer, and the government. If an audit originates in the Internal Revenue Service Center correspondence division, it can be transferred to a local district office. Also, if the taxpayer receives a letter from a district office that is not convenient to them presently, they can request a transfer to a district office closer to them. The transfer request should only be made if the taxpayer has moved from the area in which the tax return was originally filed or if the records are in a different area, e.g. an accountant's office, and are too voluminous to mail. This allows us to assist our clients, regardless of where they live.

One last note on audit selection is the audit cycle or year. Tax returns generally are selected and audit letters are sent out to taxpayers from October 1st of the year in which the

continued page 3

The material in this newsletter is general in nature and no final conclusion on the technical matters discussed herein should be made without further review and consultation.

ENTERTAINMENT FACILITIES

by Bob Nelson

As a tax and financial counselor for Alan Fields and Associates, I am asked quite frequently about available deductions for entertainment facilities.

Entertainment facilities encompass a wide range of areas. Such areas include: boats, lodges, camps, summer homes or condominiums, vacation cottages, hotel suites, country clubs or similar social, athletic or sporting club or organization, bowling alley, tennis court, swimming pool or other similiar property.

As self employed distributors, we are affected by three sections of the Internal Revenue Service code.

The allowance of all ordinary and necessary expenses directly related to your business is covered by section 162. The second section which affects us is section 274. This places limitations on business entertainment expenses, gifts, foreign and domestic travel. This code section establishes record keeping requirements. The third section, code section 280 A, disallows deductions taken for personal use of a home, apartment, condominium, mobile home, boat or other similiar property

continued page 3

TAX AUDIT SERVICE

The IRS Enrolled Agents, employed at Alan Fields and Associates are fully qualified, and highly experienced to legally represent you on all IRS Tax Audits. We can also be of service to you in any other governmental audits. When you have need for competent audit representation, be sure to call Alan Fields and Associates 213-986-3405 (outside Los Angeles, call collect).

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EDITORIAL "TAX-SIDE" CHAT

This year is already half over, and it is important to remember that your tax planning should go on all year. I have seen people become extremely upset if they face a large tax bill on April 15th, and yet they made no attempt to do any planning during the year. It becomes even more important to do tax planning if you have any significant changes in your financial condition during the year. For example: a new job; change in marital status; a new child or a child no longer qualified as a dependent; sale or purchase of property; sale or purchase of a business; receiving a large bonus; receiving a distribution from a retirement plan; large capital gain or loss; or any other major change.

The new administration has proposed some broad and sweeping tax changes that will affect all segments of the economy. It becomes even more critical this year than ever before to do year 'round tax planning. The changes have not become law yet, but let's discuss some of the more promising changes.

A proposed change in the tax rate structure will produce an across the board tax cut to the extent of 1.25% in 1981 (this is actually a 5% cut effective October 1, 1981). There would be a further 10% cut effective July 1, 1982 with another 10% cut on July 1, 1983. In addition to these cuts, the present 70% top tax rate on unearned income (e.g. interest, dividends, taxable portion of capital gains, etc.) would be reduced to 50% effective in 1982. The Democratic members of the House Ways and Means Committee have agreed in principle to all except the proposed 1983 cut. These cuts and the reduction in the maximum tax rate may have the effect of making some tax shelters less attractive, and the importance of municipal bonds or other tax exempt securities should diminish.

Some of the administration's other proposals include: relief from "the marriage penalty" (the extra tax two people pay when they have to file jointly instead of as two singles); raising the maximum contribution to an IRA (individual retirement account) from the current $1,500 to $2,000, up to 100% of an individual's earnings for the year; increasing the present maximum deductible contribution to a Keogh Plan from $7,500 to $15,000; allowing faster depreciation on real estate; raising the annual gift tax exclusion per donee to $10,000 from the present $3,000; and increasing the estate tax credit so that by 1985 an estate up to $600,000 (including the value of a direct sales business) will be entirely free of Federal Estate Taxes. These changes will make Real Estate Rentals a more attractive investment, make it easier to save for retirement, and less costly for an estate to go to your heirs.

Not all tax changes this year are coming from the administration, a RECENT COURT CASE may prove to be very beneficial for those of us in the Direct Sales Field. In order to claim a deduction for office-at-home expenses you must use a portion of your home exclusively for business. IRS has defined a portion of your home to mean an entire room or an area with partitions. But, in George H. Weightman, TC Memo 1981-301, the Tax Court disagreed with IRS on this point. Mr. Weightman had a specific area of his bedroom furnished with a desk, a chair, two file cabinets, and three bookcases. A bed and dresser were located in the other part of the room. The Court agreed that "there was, in fact, some separate, though unmarked, area that he used exclusively and on a regular basis as his home office." The court was convinced that there was a separate area of the bedroom used exclusively as a home office. Because Mr. Weightman's home was not his primary place of doing business, the Court did not allow him the deduction. But, this new interpretation of exclusive use will make it easier to receive a deduction in your Direct Sales Business.

Alan Fields

TRAVEL TALK

by Peb Conrad

At the free tax workshops I have conducted, a question that arises quite often is, "How do I need to substantiate and prove that my travel was for business?"

As a self employed person, the expenses incurred in business related travel are tax deductible. In this article we will be using the term distributor to refer to a self-employed person, whether: a single individual, a married couple or a partnership.

In order to substantiate business travel, it is necessary to keep certain records.

In your diary or calendar you must record the amount of expenses for meals, taxis, buses, tips, entertainment, lodging, gifts and any other expenses.

In addition, mark on your calendar, the dates and locations of your travel, entertainment, or use of entertainment facilities.

Also, you must document the business reason for the expenditure and the business relationship of the recipient of entertainment and gifts.

Besides documenting all the above information, you must keep receipts for transportation: buses, taxis (don't be ashamed to ask for a receipt), lodging, meals and other major expenses.

Not only must you keep records to substantiate your travel expenses, you must also provide proof that the trip was business related. In order to fulfill this requirement, you must provide the following information.

You will need to document the dates of the trip (both total and actual business days) and the area or destination traveled. Also record the business reason and benefit to be derived or anticipated to be derived from the trip.

Additional support of the business nature of your trip can be established by sending business

continued page 3

FREE TAX REVIEWS
1978 – 1979 – 1980

If you, or any of the distributors in your group, feel that you did not get all of the tax benefits available from your business, call us for an appointment to have your tax return reviewed by one of our tax advisors. There is no charge for this review. If, after the review, you would like us to correct your tax return, we will do so at our regular fee.

CLIENT QUESTION AND ANSWER COLUMN

by Andy Smith

Q: Why didn't I get as large a refund this year as last year?

A: There are many reasons why your refund could be less this year in comparison to last year. Some of these reasons can best be expressed through the following example.

Given the following facts:

1979: A married couple with 2 children makes $25,000 per year, has $4500 Federal income tax withheld, and has no itemized deductions. Only the husband works, while the wife stays home. The refund that they are entitled to is approximately $1000. This is typical every tax year.

1980: The same couple with 2 children can't make ends meet in these inflationary times, therefore, the wife goes to work. The husband is still making $25000 salary with $4500 Federal income tax withheld, while the wife makes $10,000 with $1800 Federal income tax withheld. In addition, they started their own business that created a loss of ($1900). This yields a refund of approximately $400.

The taxpayers want to know why they are getting back so little. Discussing the above situation, the husband makes his usual salary and has the same $4500 of Federal income tax withheld. The wife makes $10,000 and has her employer withhold the maximum amount of Federal income tax withheld, while her husband is claiming married with 4 exemptions with his employer. The couple was not concerned about their tax situation because of the anticipated loss on their new business. What has happened here is that each employer is withholding Federal income tax as if that was the only income being earned. In other words, the husband's income is withheld at a 21% tax rate, while the wife's income is withheld at an 18% tax bracket. Combining their income with their business loss, they are taxed at a 32% tax bracket. This happens quite often, and is not usually planned for. This all could have been alleviated by seeing your tax consultant, when your tax situation changed.

There are other tax situations that can and will occur such as increases or decreases in your business losses, investment tax credit, income averaging, sale of assets, etc.

FREE TAX WORKSHOPS

The former IRS agents and auditors employed at Alan Fields and Associates are fully prepared to hold a Free Tax Workshop for you and your group at your location. This Free service has proven to be a fantastic sponsoring and motivational tool. The workshop functions best when there are between 15-35 people in attendance. Please call Alan Fields and Associates at 213-986-3405 (outside Los Angeles - call collect) to set up an appointment. You will find this program really exciting and enlightening, and it can be held during the weekdays or week nights.

Entertainment (con'd)

or dwelling unit. This code section also establishes certain exceptions to the law, such as the home office deduction when a portion is used exclusively and on a regular basis.

An expense may qualify as ordinary and necessary but if the record keeping requirments and business purpose are not met then the deduction will be disallowed. Further, if the expense meets the ordinary and necessary requirement but is determined to be a dwelling unit used as a residence it still may be disallowed as an expense.

If you use the unit to entertain prospects, associates or customers then the expense is ordinary, necessary and directly related to your business. The first section (section 162) is satisfied.

The next section (Sect. 274), states that an entertainment facility is tax deductible, if the taxpayer can establish that the facility was used primarily for the furtherance of his trade or business, and that the expenditure was directly related to the active conduct of such business. The main factor is not the intended use of the property, nor what it is available for, but what you actually use the property for.

continued page 4

Audits (con'd)

tax return was filed until September 30th of the following year. As an example, audits for 1980 Federal tax returns will commence October 1, 1981 and continue until September 30, 1982. An individual audit may extend beyond these dates, but most audits are initiated during this period of time.

Travel (con'd)

correspondence in advance to prospective or established distributors.

If you need help setting up the format, contact any of the counselors at Alan Fields and Associates.

Persons with a direct sales business who are operating their business as a corporation and therefore are employees of the corporation, or have a partnership and are being treated as an employee of the partnership, fall under different reporting requirements for travel substantiation.

As the owner, you should establish travel reimbursement and expense policies and guidelines for "employees" of your business (this includes yourself).

For our purposes we will assume that all travel (and entertainment) expenses of the employee are reimbursed in full by the corporation or partnership. You, as the employee, must account to the corporation/partnership by submitting expense account books, diaries, statement of expenses, receipts or other records shortly after the expenses are incurred. These records should include the same information as a person self employed. For your own tax records, you must account for all reimbursements, travel advances or other expenses inclusive of the use of your employer's credit cards.

As a "owner-employee" in this situation you may be asked to substantiate your travel expenses even though you have reported it to your "employer" in the event your return is audited.

If as a "distributor" or "employee" you follow these requirements of substantiation and proof of business activity, we at Alan Fields and Associates believe you will have met the guidelines for establishing your travel tax deductions.

Entertainment (con'd)

The primary use is established by verifying (usually by diary or other similiar records) that over 50% of the use of the facility during the taxable year was business use. In the case of an automobile it would be miles, for a plane it would be hours, and for boats, lodges, camps, summer homes or condominiums, vacation cottage, hotel suite, country club, tennis court, swimming pool, or other similiar property it would be calendar days.

Any day the facility was used for the conduct of a substantial and bona fide business discussion, or used primarily for the furtherance of your business in an ordinary and necessary relationship to your business, then it would be considered a business day. The facility may have also been used for personal or family use on that same day, and still qualify as a business day.

An allocation of deductible expenses related to the facility would include: depreciation, all operating costs including rent and utilities, repairs and maintenance, painting, insurance, salaries to gardeners, caretakers or watchmen, losses on the sale or other disposition of the facility, and any other related dues paid monthly, yearly, etc.

Code section 280 A states that no deduction is allowed with respect to the business use of a dwelling unit that is also used as a residence. A taxpayer, who uses such unit the greater of 14 days or 10 percent of the number of days during the year the unit or facility is rented, is deemed to have used it as a residence.

There is a current conflict with the Internal Revenue Service as to specifics on what consitutes a personal days use. There have not been any regulations for this code section which have been prescribed. Can a person travel and stay ovenight in a rental condominium that he owns, that needs his personal attention for repairs and cleaning, and not have the overnight stay treated as a personal day? The IRS has lost on their position to treat this as a personal day and again it would seem that if business was conducted any part of the day, it would be in fact a business day.

Here are some examples that show the interaction of these three code sections. Assume you have a swimming pool that was used 56 times during the year. All days used were documented. Out of the 56 days it was used, there were 13 days that it was used personally with no business relationship and the remaining 43 days usage were all strictly business days, where you either prospected an individual, discussed some commercial accounts, sold products or just gathered information about someone you felt would strengthen your organization. We have met all the requirements of the law here and could claim 76 percent (43/56) of all the related operating expenses of the swimming pool.

For the next example, you own a mountain cabin up in Big Bear. During the year you stayed up there for 13 different weekends. During each weekend stay you entertained prospects, presented the plan, and also had product demonstrations. Since the activities are ordinary and necessary and directly related to your business and since you documented all the weekend activity in your diary, you have met the first two sections of the law. Now if you performed these business activities on each of the total of 26 days, then you could claim 100% of all documented related expenses. If the IRS were to consider (for the purposes of code section 280 A) the night that you stayed over as a personal day, the total personal days would only amount to 13 and you could still claim the deductions.

For more detailed information regarding this topic, please feel free to call me or any of our other counselors at Alan Fields and Associates.

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HIGHLIGHTS OF ECONOMIC RECOVERY TAX ACT

by Andy Smith

The following excerpts are some highlights of the 1981 Economic Recovery Tax Act that will directly affect you today and tomorrow.

With the new tax law, there will be a 1¼% reduction in tax rates for individuals in 1981, 10% reduction in 1982, 19% reduction in 1983, and 23% reduction in 1984. It would be good tax planning to maximize your deductions currently and defer any income to the next year, when the individual tax rates will be 8¾% lower. Below is a current joint return tax rate chart that illustrates the reduction in taxes for the next four years.

con'd page 4

	1981 (pre-credit)		1982		1983		1984	
Taxable income bracket	Tax at low end of bracket	Tax rate on income in bracket	Tax at low end of bracket	Tax rate on income in bracket	Tax at low end of bracket	Tax rate on imcone in bracket	Tax at low end of bracket	Tax rate on income in bracket
$0-$3,400	$0	0%	$0	0%	$0	0%	$0	0%
$3,400-$5,500	0	14	0	12	0	11	0	11
$5,500-$7,600	294	16	252	14	231	13	231	12
$7,600-$11,900	630	18	546	16	504	15	483	14
$11,900-$16,000	1,404	21	1,234	19	1,149	17	1,085	16
$16,000-$20,200	2,265	24	2,013	22	1,846	19	1,741	18
$20,000-$24,600	3,273	28	2,937	25	2,644	23	2,497	22
$24,600-$29,900	4,505	32	4,037	29	3,656	26	3,465	25
$29,900-$35,200	6,201	37	5,574	33	5,034	30	4,790	28
$35,200-$45,800	8,162	43	7,323	39	6,624	35	6,274	33
$45,800-$60,000	12,720	49	11,457	44	10,334	40	9,772	38
$60,000-$85,600	19,678	54	17,705	49	16,014	44	15,168	42
$85,600-$109,400	33,502	59	30,249	50	27,278	48	25,920	45
$109,400-$162,400	47,544	64	42,149	50	38,702	50	36,630	49
$162,400-$215,400	81,464	68	68,649	50	65,202	50	62,600	50
$215,400 and over	117,504	70	95,149	50	91,702	50	89,100	50

DEPRECIATION CHANGES

by Bob Nelson

Some exciting incentives in the area of depreciation have been given to taxpayers who own and operate their own businesses.

Property placed into business use after 1980 can be written off under the new "Accelerated Cost Recovery System" (ACRS) faster than under the old pre-1981 depreciation rules. ACRS virtually eliminates disputes with IRS over the number of years of useful life of business assets and their salvage values.

Basically, what ACRS does is put all depreciable property or assets into four separate categories having respective lifes of 3, 5, 10 and 15 years. Between now and 1985 a specially computed accelerated depreciation schedule based on a 150% declining balance rate can be used. For 1985 the rate would be at 175% and after 1985 a 200% declining balance rate.

This means that for an automobile having a useful life of 3 years placed into use during December 1981 a taxpayer can write off 25% of the cost in 1981, 38% in 1982 and 37% in 1983.

Property that can be written off in three years includes autos, light-duty trucks, office equipment such as calculators, typewriters and other personal property of this nature.

con'd page 3

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EDITORIAL "TAX-SIDE" CHAT

Things have been very exciting at Alan Fields & Associates. On August 10th the California Corporations Commissioner approved our permit to sell $1,000,000.00 worth of stock in our company. A limited amount of stock is available to California Residents who meet certain income and net worth requirements. If you are a California Resident and would be interested in owning shares of Alan Fields & Associates Corporation, call (213) 986-3405 or write for a copy of our prospectus.

The response to our "FREE WORKSHOP" program has been fantastic. In July and August alone, we conducted 94 Tax Workshops with over 3800 distributors and prospects in attendance. If you would like one of these fantastic motivational and training program for your group, free, call Peb Conrad at our main office.

This year has also been fantastic for Nancy and I in our direct sales business, we broke off our second Direct Distributor and see several more in the next few months. It is really great to be associated with that tremendous corporation in Ada. Our sights are set for Diamond.

Our telephones have been really jumping off the hook since the new Tax Act was signed into law. Several of the articles in this issue of the newsletter are devoted to the new tax laws, and we will provide more information as it becomes available.

The 1981 Economic Recovery Tax Act is a first step towards reducing the stranglehold of the old tax laws that did nothing more than discourage the economic productivity of the American Taxpayer. The Tax Act is a step in the right direction, although for most taxpayers the tax savings will be negligble.

For those taxpayers involved in the direct selling field and in other businesses, the tax savings may be greater. The faster depreciation and shorter times required for investment tax credit may prove to be one of the largest tax savings area for self-employed individual.

There are several things that you can do to maximize your tax savings under the new Tax Act. The first real impact of the reduced tax rates will not be felt until 1982, so get as many deductions in 1981 and push as much income into 1982 as you can. For example: pay both halves of your property tax bill in December; make an extra mortgage payment or other interest payment before the end of the year; make charitable contributions in December instead of January; repair or paint rental properties before the end of the year; buy a business automobile this year instead of next; pay for 1982's business travel or seminars this year instead of in 1982; purchase business supplies in 1981; don't sell capital gains property in 1981 if you can wait until 1982; take year-end bonus in January 1982 instead of December 1981 if your employer permits. There are many other techniques you can use, so don't hesitate to call us to discuss your personal situation.

Alan Fields

LEASE OR BUY YOUR AUTO

by Bob Frome

A question which comes up quite frequently is, "How does an open end lease differ from a closed end lease?" An open end lease provides that if the Fair Market Value (FMV) of the car at the end of the lease period is higher than the value computed in the lease you will receive a refund of the excess paid. Conversely, with a closed end lease if the FMV is higher you will most likely receive no refund. An additional difference is that with an open end lease the value of the car at the end of the lease period is put at a dollar amount close to the estimated FMV based upon prior experience in the market place while the closed end lease value is usually substantially lower than the estimated FMV which will result in higher lease payments.

With both types of leases if the actual value of the car is lower than the initially established value you would have to pay the difference. Both types of leases most often provide for an option to purchase the leased automobile for the initially established value.

In addition, clients ask if they will receive investment tax credit for leasing an automobile.

There is one instance when a leased car will qualify for ITC. The law permits the leasing company to make an agreement in advance to pass the ITC through to you. This allows you to claim the ITC the leasing company would have otherwise qualified for. This is normally called a "pass through lease" and must be included in the original contract. In addition, if you have a leased car which you later purchase, it will not qualify for ITC.

Depreciation is another factor to consider when leasing. With a lease neither depreciation or the standard mileage rate may be claimed. If at the end of your lease you decide to exercise your option and purchase the automobile, from that point on depreciation may be claimed.

If leasing you are allowed actual expenses of the use of the car. A simple way to determine this is by looking through your mileage log (a diary everyone should be keeping), and determine what percent of your total mileage for the year was business related. If your total mileage for the year was 10,000 miles and your business mileage is 8,000 miles, then 80% of your monthly lease payment would be deductible. Also 80% of the operating expenses, e.g. gas, oil, insurance, repair, and maintenance are deductible. The sales tax paid on a leased automobile is added to the monthly payments and is deductible in the year paid.

con'd page 4

The material in this newsletter is general in nature and no final conclusion on the technical matters discussed herein should be made without further review and consultation.

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ALL SAVERS CERTIFICATES

by Bob Frome

The new law provides for a once-in-a-lifetime exclusion of up to $1000 ($2000 on a joint return) of interest earned on a one-year tax exempt savings certificate issued by a bank, savings and loan or similar institution. This will have an interest yield equal to 70% of the yield on 52 week Treasury bills. The Certificate must be issued after September 30, 1981 and before January 1, 1983. All exempt interest must be earned before January 1, 1984. This means, that if a married taxpayer earns $400 of exempt interest in 1981 and another $1600 in 1982, the exclusion is exhausted and the taxpayers can exempt no further interest in 1983.

The exclusion will not be allowed in any year in which there is a premature withdrawal or if the certificate has been pledged as collateral.

Caution should be exercised before investing in an All-Saver Certificate. Based on the current Treasury Bill rate, the All-Saver Certificate would yield 12.61%. An analysis should be made to determine the effective taxable rate based on your bracket.

EXAMPLE: 1982 Rates

Taxable Income	Federal Tax Bracket	Effective Taxable Yield
12,000	19%	15.57%
20,000	25%	16.81%
25,000	30%	18.01%
35,000	40%	21.01%
50,000	50%	25.22%

You should compare the Effective Taxable Yield to the yield of other investments.

To earn the maximum $2000 for joint filers based on 12.61% you would need a deposit of $15,861. For single filers a deposit of $7,931 would be needed to earn the maximum $1000.

The consultants at Alan Fields & Associates are advising clients to wait until October 2nd to invest in the All-Savers. There will be a new Treasury rate on October 1st, which will affect All-Savers on October 5th. Consequently, if the new rates goes up, the investement should be made on October 5th. However, if the new rate goes down, the investment should be made on October 2nd, that way the investor will receive the higher rate for the full year.

This advertisement is neither an offer to sell nor a solicitation of offers to buy any of these securities. The offering is made only by the Offering Circular. The offering is made only to California Residents who must meet the financial requirements described in the Offering Circular.

100,000 Shares

ALAN FIELDS & ASSOCIATES

Common Stock

Price $10 Per Share

Copies of the Offering Circular may be obtained from the officers and directors of Alan Fields & Associates at 14011 Ventura Boulevard, Suite 306, Sherman Oaks, California 91423. (213) 986-3405.

Depreciation Changes

(continued)

Five year property would include other personal property having a normally longer useful life such as computer equipment, heavy machinery and the like.

Ten year property includes real property that under the old methods had a useful life of up to 25 years.

15-year property would be all other real property (buildings) that under the previous methods had a useful life of 25 years or more.

All business property placed in service prior to 1981 must continue to be depreciated as under pre-1981 law. Transfers of this property in exchanges, lease backs and between related parties will not allow the new owner the opportunity of using the new "Cost Recovery" methods for depreciation purposes.

Taxpayers aren't required to use the 3, 5, 10 and 15-year recovery period categories or the Accelerated Recovery Schedules. They can instead use longer lives but would be limited to the straight line depreciation method. Taxpayers also have the option of using straight life depreciation with the 3, 5, 10 and 15-year lives.

Because of these changes regarding personal depreciable property, there have been changes made in the area of investment tax credit that affect individuals owning businesses.

INVESTMENT CREDIT RULE CHANGES

For personal property used in business and placed into use during 1981, the investment credit percentage for property which uses the new "Accelerated Cost Recovery System" (ACRS) is, with respect to 3-year recovery period property (an example would be an automobile), 6% and for 5, 10 and 15-year recovery period property, 10%. If the asset is disposed of before its proper useful life, the credit is recomputed on early disposition by allowing a 2-percent credit for each full year since the property was placed in service. In the year on early disposition the unallowed credit must be added back to the tax. Thus, no recapture is required for eligible 5-year, 10-year or 15-year property actually used in the business for at least 6 years, or for eligible 3-year property held for at least 3 years.

EXAMPLE: Let's say that you acquired either a new or used car and paid $10,000.00 for it. Under the (ACRS) guidelines it qualifies as a 3 year asset, therefore you would be entitled to a 6% investment tax credit on the percent used for business. If the taxpayer could establish that he used the car 90% of the time for business he would receive the following credit:

Cost	10,000
Percent business	.90
Business basis	9,000
Allowable credit	.06
TOTAL ITC	540

Under prior law with a 3 year useful life the taxpayer would only get a $300.00 credit so you can see that the new tax law gives us some additional benefits.

Economic Recovery Tax Act

(continued)

IRA & KEOGH PLANS

The major changes for taxable years beginning after 1981 are 1) A participant in an IRA plan may deduct the lesser of $2000 or 100% of compensation; 2) An increase from a maximum of $1750 to $2250 has been approved for a spousal IRA; and 3) An employee may now have an IRA account, even though he is active in a qualified pension plan. Keogh plan contributions have been increased from a maximum of $7500 to $15000.

ESTATE TAX

You no longer have to include gifts made by decedents within three years of death in their gross estate, but must include it for purposes of determining whether the estate qualifies for current use valuation, deferred payment of estate tax, and qualified redemptions to pay estate tax.

GIFT TAX

An increase from $3000 to $10,000 per donee and $20,000 in the case where an election to split gifts is made by a married couple. This allows you to transfer more of your assets free of gift or Estate tax.

FALSE WITHHOLDING CERTIFICATES

Be cautious when you file your next W-4 (withholding certificate). Your employer is required to report to the Internal Revenue Service, if you claim more than 9 withholding allowances. The Internal Revenue Service will scrutinize those W-4's submitted and probably more so now, because of the current change in penalty for filing false withholding information. The penalty has been increased from $50 to $500 beginning in 1982. Also the penalty is increased to $1000 for willfully failing to supply information, or for willfully supplying false or fraudulent information in connection with wage withholding.

INTEREST AND PENALTIES

The interest charged by IRS for tax due is to be 100% of prime as of September, 1981 with annual adjustments beginning January after February 1982.

If negligence is determined during an audit with tax due, there may be additional penalties of 50% of the interest charges on the deficiency as well as a penalty of 5% of the tax due.

Further, if a valuation overstatement results in a tax deficiency, the taxpayer may be liable for as much as an additional 30% penalty based on the tax due as a result of such overstatement.

Lease or Buy Your Auto (con'd)

Because the tax benefits of leasing or purchasing a business automobile have a significant impact on your tax situation, it is important to carefully analyze each before making a determination.

If you have a question regarding your personal situation, all of us at Alan Fields & Associates would be glad to help you determine which is the best option for you.

FREE TAX REVIEWS
1978 – 1979 – 1980

If you, or any of the distributors in your group, feel that you did not get all of the tax benefits available from your business, call us for an appointment to have your tax return reviewed by one of our tax advisors. There is no charge for this review. If, after the review, you would like us to correct your tax return, we will do so at our regular fee.

Alan Fields & Associates maintains a full time office in Sherman Oaks (213-986-3405-outside 213 call collect) to aid you in all aspects of tax preparation, tax reviews, professional representation at audits, bookkeeping, and a host of other financially related activities. Our staff consists of active distributors who are former Internal Revenue Service agents and auditors. This past tax season we operated satellite offices in Ventura, Long Beach, Palmdale, Redlands, Sacramento, San Diego, San Francisco and Fresno. We are now planning to expend our office locations throughout California and other Western States. We certainly look forward to being of service to you.

ALAN FIELDS & ASSOCIATES
TAX NEWSLETTER
14011 Ventura Boulevard, #306
Sherman Oaks, California 91423

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ALAN FIELDS & ASSOCIATES TAX NEWSLETTER

Published as a service to our clients and business associates

OCTOBER/NOVEMBER, 1981

14011 VENTURA BOULEVARD
SHERMAN OAKS, CALIFORNIA 91423

(213) 986-3405
(call collect outside the 213 area code)

HOME OFFICE

By Bob Nelson

Many of you are claiming a home office deduction. However, there is a limit to the amount that can be claimed as a home office deduction. That limitation is equal to your Gross Business Income (retail and wholesale sales, performance bonus received, contest and incentive awards, speaking fees, etc.) minus those allocable deductions that are allowable regardless of qualified use. (These deductions include interest, taxes and casualty losses.)

Here's an illustration of how this limitation is applied:

John Jones uses 20% of his personal residence as a qualifed home office. He pays $1,500.00 in mortgage interest and $500.00 in real estate taxes. John grossed $10,000.00 in income from his business which includes retail and wholesale sales and also some performance bonuses. John would compute his income limitation as follows:

Gross income derived from business	$10,000
Less: Allocable portion of interest & taxes	
$1,500 + $500 = $2,000 x 20% =	(400)
Home office deduction limitation	$ 9,600

Remember, this is the computation for the limitation only. The allocable home office deduction cannot exceed this limitation!

In order to qualify for a home office deduction the area that is used exclusively must also be used "on a regular basis". There are no specific guidelines or written explanation to define this, however, in the proposed regulations it states that "The determination must be made in light of all the facts and circumstances." So you can see that the amount of business use can be minimal, even as little as once a week.

EXPANSION IN PROGRESS

Alan Fields & Associates maintains a full time office in Sherman Oaks (213-986-3405 outside 213 call collect), to aid you in all aspects of tax preparation, tax reviews, professional representation at audits, and a host of other financially related activities. Our staff consists of distributors who are also former Internal Revenue Service agents or auditors.

We will be doing tax preparation in the following geographic areas during the upcoming tax season:

San Diego
Mission Viejo
Santa Ana
Long Beach
West Los Angeles/
South Bay area
San Gabriel Valley
San Bernardino
Apple Valley
Antelope Valley
San Fernando Valley
Ventura/Oxnard
Santa Barbara
Santa Maria
Bakersfield
Fresno
San Jose
San Francisco
Bay area
Sacramento
Lake Tahoe

In addition to the above California locations, we will be operating in the following states; where locations are presently being evaluated and will be announced shortly:

Washington
Oregon
Nevada
Colorado
Arizona
Texas
Illinois

In addition, as a service, we will send a tax specialist to other locations throughout the Continental United States, for a group of 25 or more appointments.

• • •

Please call now to reserve your appointment to have your 1981 tax return prepared.

213-986-3405 outside L.A. call collect

TRAVEL TALK

by Peb Conrad

We at Alan Fields & Associates are frequently asked how much business activity is necessary while traveling to qualify for a tax deduction. This issue we will discuss Domestic Travel (50 states & District of Columbia) and Domestic Conventions (including U.S. possessions, Puerto Rico and trust territories of the Pacific).

If you take a trip and conduct business, you will fall within one of four basic categories depnding on the primary purpose of the trip.

1. For a trip which is entirely for business you may deduct all your "ordinary and necessary" expenses.
2. If the trip is "primarily" business but has personal "non-business activity" days interspersed you may again deduct all ordinary and necessary expenses related to the business including the meals and lodging for those non-business days but not the expenses for pleasure, sightseeing or non-business transportation.
3. If a trip is "primarily" business and while on the trip you extend your stay for vacation or travel to

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EDITORIAL "TAX-SIDE" CHAT

There are still distributors promoting the marketing plan as a TAX SHELTER. The plan conceived in Ada, Michigan is not a tax shelter, but rather is a system that enables persons from all walks to life to establish a business for themselves and their families. It is the tremendous income potential of this business that gives the ability for those distributors actively building their business to generate tax deductions for themselves.

Those distributors who go year after year without any real attempt to build their business, and want to take large tax deductions, are only fooling themselves. Those distributors who come into the business merely to buy products for their own use, and expect to get tax benefits, are also kidding themselves. And those distributors who refuse to document business activities in their diary or neglect to keep business expense receipts will also pay more income tax than they expected.

In order to claim the tax deductions that you have heard about, you must show enough business activity to establish a profit motive. There are no hard and fast rules for the amount of business activity necessary, but if I were still an IRS Agent, I would expect a distributor to at minimum: 1) Strive to reach a new Performance Bonus Bracket at least every two months; 2) Personally sponsor an average of one new distributor each month; 3) Retail consistently each month; and 4) Personally use the products. If you are not accomplishing this right now, then get together with your sponsor or direct distributor to learn the methods and techniques necessary to build the business.

IRS Agents and Auditors are a lot smarter than you may think. They will not allow you to convert your commuting expense into a business deduction if you don't actively build, and if you aren't actually engaged in business activities prior to leaving and after returning home. Don't try to write off a vacation trip if you aren't going to conduct business. Make sure you actually show the marketing plan while on the trip. Writing off a vacation trip to Hawaii because you are going to prospect for your business is not likely to be a valid deduction. But if you go to Hawaii, show the business and sign up a number of distributors, you shouldn't have any problem. Taking a tax deduction for Christmas or Channuka gifts is great, but IRS is not going to allow it if you don't either go back and show those people the marketing plan or offer to service them the products. The same applies to entertainment expenses.

In order to help you qualify for the tax deductions you want, and to help you properly use tax benefits as a sponsoring and business building tool, the entire Alan Fields & Associates Staff is here to act as a TAX SUPPORT SYSTEM for your business. We have developed a number of SUPPORT PROGRAMS designed to educate and motivate the distributors in your group. These programs are offered free of charge to all distributors associated with that great corporation in Ada, Michigan. It is our belief that by helping you build your business, our business will also grow.

This NEWSLETTER is one such program. Published bi-monthly, each issue covers items specifically related to your business as well as general tax topics. Any U.S. Distributor can be added to the newsletter mailing list by phoning or writing our main office.

Our TAX WORKSHOPS are another excellent program. Designed for groups of 15 to 45 distributorships, these workshops will educate your distributors on the tax benefits available through their business as well as recordkeeping, and activity requirements. These workshops include a question and answer session, and are done in a motivational style suitable for even the newest distributor.

A third program is our TELEPHONE TAX COUNSELING for any distributor, or even a prospective distributor. Call us at (213) 986-3405 any Tuesday or Thursday, between 9:00 A.M. and 5:00 P.M. Pacific time, and we will be happy to discuss any tax matters or answer any tax questions for you on the phone. Not all questions can be answered over the phone, but we will try to answer your question if possible.

In addition to the free services, Alan Fields and Associates provides the highest quality Tax and Financial Planning assistance available. We are Direct Sales Specialists providing expert Tax Preparation Services throughout the United States. All of our Tax Counselors are Former IRS Agents or Auditors. Our Enrolled Agents can and do legally represent distributors in all Audit Situations, whether or not the return was prepared by us.

We are constantly looking for ways of improving and expanding our services for you, and welcome your suggestions.

As one additional service for you, if you are calling us from outside the (213) area code, whether for free or fee services, don't hesitate to call us collect. Remember, if you are a distributor then we are your TAX SUPPORT SYSTEM.

Alan Fields

CLIENT QUESTION AND ANSWER COLUMN

By Andy Smith

Q. Do I need to make quarterly estimated tax payments?

A. As explained in Internal Revenue Service Publication 17, page 27: "You must file a declaration of estimated tax using form 1040-ES, 1981 Declaration-Voucher, if your estimated tax is $100 or more and: 1) your expected gross income for 1981 includes more than $500 in income not subject to withholding, or 2) your expected gross income is more than: a) $20,000 if you are single, a head of household, or qualifying widow or widower, or b) $20,000 if you are married, entitled to file a joint declaration, and your spouse has not received wages for 1981 or c) $10,000 if you are married, entitled to file a joint declaration, and both of you have received wages for 1981, or d) $5,000 if you are married and not entitled to file a joint declaration."

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FREE TAX REVIEWS 1978 – 1979 – 1980

If you, or any of the distributors in your group, feel that you did not get all of the tax benefits available from your business, call us for an appointment to have your tax return reviewed by one of our tax advisors. There is no charge for this review. If, after the review, you would like us to correct your tax return, we will do so at our regular fee.

TAX AUDIT PROCESS

by Jack Closson

In previous issues we discussed audit selection processes. This month, for the few of you who may be audited, we will discuss preparing for a tax audit. If your return has been selected for audit by the Internal Revenue Service Center, it is forwarded to the District Headquarters Office closest to the address on the tax return. From that office, it is sorted and sent to the closest local district Office. For example, if you live in Santa Monica, CA. and list that address on your tax return, the return would go from Fresno IRS Center to Los Angeles District Office to the West Los Angeles Post of Duty office.

Once the local office receives your file, you will also receive a letter notifying you that an audit is being conducted, defining the issues or areas to be audited, and explaining the procedures and your rights under the law. The letter will either set the time, date and place of the audit or ask you to call for an appointment. It is at this point that normally rational humans break into hysterics and complete confusion.

The easiest and most logical course is to pick up your telephone and call our office or your tax preparer. It is at this point that you will need questions answered and professional advice.

In most cases, the audit is a simple process of showing a few receipts or a year-end statement to prove contributions, interest, etc. However, you should consult with a professional who understands IRS procedures and can advise you of the course of action to take.

In a great many cases, it is better to have a qualified tax consultant represent you for a number of reasons: 1) psychological – you are emotionally involved if you represent yourself; 2) communication – you may not understand technical terms used by the auditors; 3) technical – you may not be aware of all the legal aspects of the areas being

continued page 4

QUESTIONS & ANSWERS (con'd)

Each individual case may change throughout the year. For example: you may purchase a $10,000 automobile to be used in your business which will yield a $1000 investment credit (assuming that the automobile is 100% business use.) In this situation, your estimated tax voucher would be adjusted to a lower amount. An example that would warrant an increase in your estimated tax payments, would be a sudden increase in income. This would come from a $10,000 bonus at the end of the year, or possibly the sale of shares of stock. There are many transactions and tax situations that may affect the amount of your estimated tax payments and you should be aware of them.

We at Alan Fields & Associates feel that a common misconception is that people can wait and make one payment with their tax return.

If you are required to make installment payments for estimated tax, you must pay these amounts on or before the following dates: April 15, 1981; June 15, 1981; September 15, 1981; and January 15, 1982. the January 15, 1982 payment is not required if you file your return and pay any tax due in full by January 31, 1982. When mailing your check or money order be sure to include your Social Security number, form 1040ES, and 8112.

If at least 80% of your tax liability is not paid to the Internal Revenue Service or State Franchise Tax Board, then the unpaid portion is subject to a failure to estimate penalty.

However, the IRS and FTB have provided four exceptions to the rule.

The most common exception would be to use last year's tax shown plus any self-employment tax. As long as you pay in the same amount this year as you paid in last year, then there is no penalty. If you want to avoid making estimated tax payments and you are a W-2 wage earner, all you have to do is make sure that sufficient amounts are with held to cover yourself.

Our counselors here at Alan Fields & Associations can provide you with expert assistance with your individual situation.

Q. I'm receiving social security benefits? How does earnings from self-employment affect my benefits?
A. Earnings from self-employment does affect your monies received from Social Security, but not the same way as an employee earning wages. An employee earning wages will have their social security benefit affected by the gross amount earned. In general, as a self-employed person, your social security benefits are adjusted based on net profits, rather than gross receipts. Always check with your local social security office regarding your specific situation.'

Footnote 1 – SSA Publication #05-10069

TRAVEL continued

another destination before returning home, you may deduct only the "ordinary and necessary" expenses related to the business portion of the trip, including transportation expenses. (eg) If you travel from Los Angeles to Chicago on business and return to Los Angeles via Las Vegas, you may deduct air fare or other transportation costs only to the extent of direct round trip cost between Los Angeles and Chicago.

4. Where the trip is primarily pleasure you may deduct only the expenses at your destination that were incurred solely as a result of business.

The primary purpose of the trip is determined by your intent. When a travel locality could be construed as a vacation, such as an area where friends or relatives live, or a vacation area (i.e. Hawaii, Orlando, San Diego, Washington, D.C., etc.) you must establish specific business contacts to show a business purpose for being in that locality. If you are visiting friends and/or relatives, whether or not they are associates or clients in the business, you must establish some documentary contact (letters, mailgram, telegram)

continued page 4

FREE TAX WORKSHOPS

The former IRS agents and auditors employed at Alan Fields & Associates are fully prepared to hold a Free Tax Workshop for you and your group at your location. This Free service has proven to be a fantastic training and motivational tool. The workshop functions best when there are between 15-45 distributorships in attendance. Please call Alan Fields & Associates at 213-986-3405 (outside Los Angeles - call collect) to set up an appointment. You will find this program really exciting and enlightening, and it can be held during the weekdays or week nights.

AUDIT PROCESS (con'd)

audited. These and other areas are complexly interrelated and can cause many individuals to pay more tax than they properly owed.

For those of you who have simple audits, you should contact the phone number on the letter to confirm or set the audit appointment. (If the audit is scheduled at an office which is inconvenient you may request a closer office.)

You should clarify the issues being audited and put your verifying documents in order. Always be prompt for your appointment and have your documents so that you can hand them to the auditor without a lot of paper shuffling. Also, give clear, concise (not wordy) answers to any questions. Be courteous to the auditor and listen intently to each question. Do not get upset if the questions appear personal or insensitive; the auditor probably doesn't like asking the question, but may need the information. However, the questions you answer should only pertain to the issues under audit. Do not allow the auditor to open new issues by asking unrelated questions.

If you can not make the original appointment, call and reschedule it. You may be allowed to reschedule 2 times if you have good reasons. Remember, the auditors will try to accomodate you, but they have other audits, time constraints and procedures they must follow. In any event, do not miss an appointment without contacting the auditor. This will cause any deductions under audit to be disallowed and a report showing additional tax due will be sent out.

Each time that you appear for an audit appointment, it may cause a report to be written. Try to reach an agreement with the auditor on your first interview, but, remember, you can appeal any decision or submit additional information before the final decision is made.

After you have submitted all of your available documentation, the auditor will issue a report showing the changes, if any, that they feel apply and the resultant tax or refund due. This may be mailed or handed to you at the end of the audit. Remember this is an individual's opinion of the facts presented based on their interpretation of the law and may be appealled.

Your rights and responsibilities will be discussed in a later issue. If you have any questions on an audit, please call our office and we will try to assist you regardless of whether or not we prepared the return under audit.

The material in this newsletter is general in nature and no final conclusion on the technical matters discussed herein should be made without further review and consultation.

TRAVEL (continued)

establishing the business reasons for the trip prior to and subsequent to the trip. If you do not have a specific business intent and cannot establish that intent it is very likely that you would not be allowed to deduct the travel expenses on your tax return.

Convention expenses can be a business deduction if you show that the convention benefits your own business. Ordinary and necessary business expenses would fall under the following categories:

a) Meals; loding; air, rail and bus fares; baggage charges; shipping; cost of maintaining and driving your car; operation and maintenance of trailer, camper or motor home; cleaning and laundry; telephone and telegraph; secretarial services; transportation costs at destination; tips related to above; other similar expenses related to the travel.

By conducting business when traveling you can gain some substantial tax deductions. Even more important, you will see your business grow! If you are planning a trip and have specific questions, don't hesitate to call us.

TAX AUDIT SERVICE

The IRS Enrolled Agents, employed at Alan Fields & Associates are fully qualified, highly experienced, and can legally represent you on all IRS Tax Audits. We can also be of service to you in any other governmental audits. When you have need for competent audit representation, be sure to call Alan Fields & Associates 213-986-3405 (outside Los Angeles, call collect).

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Chairman STARK. Thank you very much.

Our next witness is Mr. Jay Van Andel, president of Amway Corp., accompanied by John C. Gartland, director of their Washington affairs office.

I want to note with deference to Queen Juliana the late arrival of Congressman Vander Jagt and suggest this may be Holland Day in the capital.

Mr. VANDER JAGT. Mr. Chairman, I am glad you noted the presence of Holland Day. I wonder, Mr. Chairman, if I might, if the chairman might indulge me to welcome the witness to our Ways and Means Committee.

Chairman STARK. I would indeed be honored to have you introduce our distinguished witness.

Mr. VANDER JAGT. I welcome him with great pleasure because he is a good friend, but also because of the remarkable business that he has built in Michigan. As you perhaps have heard, Mr. Chairman, Michigan is a disaster area in terms of employment. It is wonderful to have a company that doesn't know there is a recession, where sales keep increasing and therefore jobs keep increasing. That is a real glimmer of light in an otherwise bleak picture in my State.

Mr. Van Andel has also devoted a great deal of his time to public service, and most recently was president of the U.S. Chamber of Commerce. Since you alluded to it, I might point out that he is chairman of the Netherlands-American Bicentennial Committee and is directly responsible for much of the nationwide festivities that will be associated with this event. So we are very honored to be able to welcome him to the committee.

Thank you, Mr. Chairman.

Chairman STARK. Thank you, Congressman Vander Jagt.

Welcome, Mr. Van Andel. I am not sure whether you were in the room at the beginning of the hearing and my opening comments. I would like to apologize to the Amway Corp. and to you, sir, for the cover of our transcript of Mr. Fields' tax tape which says an Amway tax tape. And it is my understanding that the Amway Corp. had really nothing to do with the tape, although the company may be indirectly referred to in the tape. It was neither an official or unofficial relationship, and the record will show that it was an inadvertent mistake.

We have a copy of your testimony. You may summarize it, read it, add to it or proceed as you see fit.

STATEMENT OF JAY VAN ANDEL, PRESIDENT, AMWAY CORP., ACCOMPANIED BY JOHN C. GARTLAND, DIRECTOR, WASHINGTON AFFAIRS OFFICE; AND DICK DeVOS, POLICY ADMINISTRATION OFFICE

Mr. VAN ANDEL. Thank you, Mr. Chairman.

At the risk of starting off on the wrong foot I would like to make one correction, Mr. Chairman. That is it is not Queen Juliana but Queen Beatrix who is here today. Juliana was her mother.

Second, I guess I would like to thank you for all of this advertising we are getting today, although I really didn't intend it to proceed this way.

I am Jay Van Andel, chairman of the board of the Amway Corp. With me today is John Gartland, director of the Amway Washington office, and Dick DeVos of our policy administration office.

Twenty-three years ago, my partner Rich DeVos and I started a direct selling company in our basements. Since that time Amway has grown to be one of the world's largest direct selling companies with sales at over $1.4 billion.

Amway products include items for home and personal care, auto care, commercial and institutional use, as well as cosmetics, hosiery, cookware, and vitamins. Amway also makes available hundreds of famous brand name items from clothing to rugs, from small appliances to watches, through the Amway personal shoppers service.

Amway Corp. is headquartered in Ada, Mich., and almost all Amway products are manufactured at Ada or by Nutrilite Products, Inc., our subsidiary at Lakeview and Buena Park, Calif., or in our recently acquired subsidiary, Statitrol, Inc., in Lakewood, Colo.

The company at present also distributes its products in 25 countries and territories. All Amway products are sold only through independent Amway distributors. Through the Amway sales and marketing plan, people from every walk of life have been able to establish successful, independent businesses in the direct selling industry. In a world that is growing more impersonal daily, personal selling—with its emphasis on quality products and dependable service—is experiencing an exciting rebirth.

Today, there are more than 1 million Amway distributorships worldwide; 750,000 of these are in the United States, delivering more than 350 different products right to their customers' homes. Some of these distributors are women, some men, but most are actually husband-wife teams, making Amway direct selling very much a family business. Many have chosen to use the Amway business to supplement their primary income, while others have made Amway their full-time careers. To become an Amway distributor, the initial cost is as little as $35, which is fully refundable. A person joins the world of Amway by being sponsored by a current Amway distributor.

A strict code of ethics governs the business practices of every distributor. Amway distributors build their businesses through their own retail sales and by sponsoring, training, and guiding other distributors. Amway distributors succeed as sponsors only when their sponsored distributors succeed in selling the products. Amway distributors do not pay for the right to sponsor others. There are no franchise fees or initial inventory requirements.

Once a distributor achieves a high level of sales volume through his own retail sales and the combined volume of those whom he has sponsored, the distributor becomes a direct distributor. As a direct distributor, he deals directly with the company and no longer with the distributor who sponsored him. Therefore, the majority of independent Amway distributors do not deal directly with Amway, and most likely conduct their businesses on a part-time basis.

One of the important principles of our success has been keeping the system as simple as possible—thereby maintaining little overhead and paperwork. This allows people to enter the Amway business with little or no business experience, yet enjoy the freedom of having their own business and being their own boss. As I mentioned earlier, there are thousands of people within the world of Amway. Each is individual, yet all share a belief in the free enterprise system.

In your letter of invitation to me to appear before this subcommittee, you expressed an interest in learning how Amway Corp. addresses the issue of the potential Federal tax liability of the distributors of Amway products. I would like to talk about what we have done over the years.

First, as a method of keeping in close contact with Amway direct distributors, that is the leadership of the corporation, Amway Corp. distributes a weekly bulletin called the Newsgram, which focuses attention on current information for the Amway direct distributors. Every year since 1973, Amway has dedicated one of the Newsgram issues in January to the Amway distributor's tax requirements subtitled "Your Amway Earnings and U.S. Income Tax."

This Newsgram covers the requirements for filing 1099's and the declaration of estimated taxes; it talks about the allowable deductions, stresses the necessity of keeping accurate records, and lists those expenses which may be deductible or which may provide a credit under certain circumstances.

As part of this testimony, there is a copy of this year's Newsgram on this subject, which we now call In The Forefront. This has always been printed as a separate sheet so that the distributors can keep it as a guide for preparing their taxes, and can copy it to assist other distributors.

Second, as part of Amway's Direct Distributor Manual, there is a section dedicated to taxes which again reminds the distributor of the requirement to file 1099's and provides basic tax information as to acceptable deductions in operating their businesses.

Third, when new direct distributors visit Amway for their 2-day seminar, tax responsibilities are discussed during the seminar.

Fourth, Amway puts out a monthly magazine called the Amagram to all Amway distributors. Over the years, we have continously provided updated information on distributors' tax responsibilities.

Fifth, not only is Amway Corp. actively informing distributors of their tax obligations over the years, but also, in 1980, the board of directors of the Amway Distributor Association issued a statement, a manifesto, which stated that during any presentation of the sales and marketing plan, distributors must not promote the Amway business as a tax shelter.

I should note that Amway Corp. distributes 1099 forms to each distributor with whom it directly does business, namely our direct distributors. Under the current law, a 1099 form only needs to be issued to those persons to whom we have paid a bonus of $600 or more per year. In fact, we issue such a 1099 form to all direct distributors regardless of the amount of their bonuses, even down to $1.

In addition, we instruct all of our direct distributors that they in turn must issue a form 1099 to each one of the distributors to whom they pay a bonus of $600 or more per year, and that each such distributor must in turn issue a form 1099 to each of their distributors to whom they have paid a bonus of $600 or more during the taxable year.

Like any growing organization, Amway has had different challenges come over the horizon from time to time. During the last year, we have become aware—from distributors and other sources—that some questions have arisen regarding the deductibility of expenses by Amway distributors, as well as misrepresentations of the Amway sales and marketing plan with regard to tax deductibility. Let me say now that Amway Corp. has never promoted—nor will it ever promote—the Amway sales and marketing plan as a tax shelter, or as a tax-saving device.

It has been our longstanding policy to endeavor to take immediate corrective action whenever a misrepresentation of the Amway sales and marketing plan has been brought to our attention. For example, we discovered in 1979 that there was a family trust tax scheme being promoted among Amway distributors. We immediately printed a story in the Newsgram warning the distributors not to promote this scheme. Through the years, we have constantly used the Newsgrams, special bulletins, and the Amagram magazine to apprise the distributors of matters of concern. We also immediately contact those involved and try to get them to correct or withdraw the offending material.

If the offenders are Amway distributors, we follow a set of procedures which can ultimately lead to the withdrawal of their distributorship. But our experience has been that we have been able to resolve the majority of these issues by working with the distributors involved and the leaders in the distributor force.

For example, earlier this year, we notified the distributor leaders of the misinformation contained in the Fields tape. Just recently, we surveyed the distributor leadership on their response to our notice. Of all distributors we contacted, 32 had distributed the Fields tape at one time. Thirty of them had discontinued use of the tape and destroyed all copies at the request of Amway Corp. prior to our inquiry. The two remaining distributorships have pulled the tape out of circulation immediately after our survey questions.

With regard to the alleged excess of deductions by Amway distributors, we have been working with the Internal Revenue Service regional office in Detroit, and at their request have put out a special bulletin which contains an article written by them, as well as a policy statement by Amway.

I am enclosing a copy of this bulletin as part of this testimony. Not only did we put out a special bulletin to distributor leaders, but we have also reprinted the bulletin in the Amagram magazine, which goes to all Amway distributors. Also, I have personally met with Commissioner Roscoe Egger to explain the steps Amway has taken to inform distributors of their tax liabilities.

I can assure this committee that we will continue to work with the Internal Revenue Service. I feel that within the near future, Amway will be able to clarify for the distributor force any question regarding the deductibility of expenses. It is a little like an ocean liner: The ship is moving steadily through the water, but it takes some time after you turn the wheel before the ship begins to turn. We believe it has made that turn.

We find that the vast majority of Amway distributors are sincerely interested in presenting the sales and marketing plan in an honest and believable manner. We also believe that these distributors are responsible citizens who are accounting for their income on their income tax returns and are claiming only those deductions which are permitted under the Internal Revenue Code.

Also, I believe that this committee should begin to address the complexity of the present Tax Code. More and more Americans have to rely upon tax advisors and preparers. Because of the complexity and, in truth, the ambiguity of the Tax Code, a small businessperson such as an Amway distributor cannot fully understand his tax liabilities, and therefore is completely dependent on a tax advisor. Again, a simpler code would allow the American taxpayer to fully understand his tax responsibility in a better way.

I do not see the necessity of any additional legislation, but I do feel that the IRS should and can work more closely with the responsible companies concerned in the direct selling industry to achieve compliance.

In summary, I would like to remind you of the strong position that Amway has taken, and quote from the special bulletin sent out to all Amway distributors in the Amagram:

> Amway Corp. believes that Amway distributors, as taxpayers, are entitled to claim all business expenses which are properly allowable under the Internal Revenue Code. But Amway Corp. does not condone those which are personal in character rather than true business expenses. Amway distributors should not rely upon casual remarks made by self-appointed experts as to the deductibility of certain expenditures as business expenses. Amway distributors should be sure that they are receiving tax advice from competent tax advisors, preferably certified accountants and/or tax lawyers.
>
> Representations made by so-called tax experts at tax seminars should be checked with your personal tax advisor before being claimed as allowable deductions on your personal Federal income tax return. Each January or February, Amway publishes a supplement to the Newsgram a general, instructional article about income tax matters. Amway also emphasizes the need for all Amway distributors to account for their Amway income on their income tax returns. While Amway suggests certain expenses which can be deducted from your gross income, Amway cautions that the applicability of those expenses in your particular case should be checked with your personal income tax advisor.

We fully recognize our responsibilities and those of Amway distributors, as American citizens to pay our fair share of taxes. I assure you we will continue to cooperate with the IRS in that matter.

Thank you for letting me appear today. I will be happy to answer any questions you may have.

[The information referred to follows:]

in the Forefront

Amway
SHOP WITHOUT GOING SHOPPING

Supplement to January 21, 1982
Newsgram

YOUR AMWAY EARNINGS AND THE U.S. INCOME TAX

The wise businessperson knows only too well that "no dollar you take in is ever really yours until you've gone by the tax collector." If your sole income for the calendar year 1981 was derived from your Amway distributorship and *if the net income from that business was less than $400 ($800 in the case of a husband-and-wife distributorship) for the year*, you need not file a federal income tax return. If, however, you are otherwise required to file a return because of income from other sources, then you must report your Amway earnings on your return, regardless of the amount.

Form 1099 Mandatory

As required by law, Amway Corporation is filing the IRS Forms 1099-NEC and Summary Form 1096 showing all monies paid to Direct Distributors, including Performance Bonuses, 3% Direct Distributor Bonuses, Ruby, Pearl, Emerald, Diamond, and Executive Diamond Bonuses, and Profit-Sharing Bonuses. A copy of Form 1099 is also being sent to each Direct Distributor.

Each Direct Distributor must in turn file with the IRS, by March 1, 1982, Forms 1099-NEC and Summary Form 1096 for each distributor personally sponsored by him to whom he has paid Performance Bonuses of $600 or more. He should also furnish each distributor with the appropriate copy of the Form 1099-NEC by February 1st.

Each distributor whose annual Performance Bonus Payments totaled $600 or more must receive a Form 1099-NEC from his sponsor.

Declaration of Estimated Tax—Individuals

All persons who receive income which is not subject to withholding and who anticipate that such income will exceed $500 during the coming year and that the tax on that income will be $100 or more must file a Declaration of Estimated Tax, Form 1040ES. Normally, the Declaration for the current year is filed at the same time as the annual Federal Income Tax Return for the prior year. For calendar year individuals, the first quarter payment of the estimated tax is due on April 15th (at the same time as filing of the Federal Income Tax Return); the second quarter is due June 15th; the third quarter, September 15th; and the fourth and final quarter January 15th of the following year.

If you do not file a Declaration of Estimated Tax by April 15th and determine later in the year that your income will exceed $500 for the year and that your tax will be $100 or more for that year, you must file a Declaration of Estimated Tax with the IRS on the next quarterly payment date during the year. The estimated tax is paid in the same number of installments as there are quarterly dates (April 15, June 15, September 15, or January 15) remaining in that year. For example, if you file your Declaration on June 15th, you must pay one-third of the estimated tax on June 15, one-third on September 15, and one-third on January 15th of the following year. See specific instructions on Form 1040ES.

Tax Tips

The key to making sure that you pay only that amount of income tax which you are legally obligated to pay [illegible] upon your maintaining accurate [illegible] records of your income and [illegible]. In fact, you can't begin to prepare [illegible] return in a way to receive maximum allowable deductions unless you have records to substantiate those deductions. This is vital should your return be audited at a later date by the IRS.

Your record-keeping needn't be elaborate, but it must be accurate and complete. Some distributors keep various records in large brown manila envelopes labeled "Purchases," "Car Expenses," etc. A daily diary is almost a must. Note all activities associated with your Amway business—why, where, who, when. A separate business checking account is equally valuable, out of which you should pay *all* of your business expenses. At tax time, your cancelled checks will provide documented expense records which are separate from your personal and household expenses.

The annual financial results of your Amway business, if operated as a proprietorship, should be reported for federal income tax purposes on Schedule C of Form 1040. Schedule C calls for the compilation of gross receipts. You must list *all* of your Amway income, including your Performance Bonuses, Direct Distributor Bonuses, Ruby Bonus, Pearl Bonus, Emerald Bonus, Diamond Bonus, Executive Diamond Bonus, and Profit-Sharing Bonus (both cash and Amway Mutual Fund portions). Your business expenses should then be deducted from your gross receipts, leaving your net income.

Even though a husband and wife operate their Amway distributorship as a partnership, they may still use Schedule C of Form 1040 to compile and report distributorship income and deductions. The IRS recently indicated that it would not subject such partnerships (with 10 or fewer partners) to penalties for failure to file Form 1065, U.S. Partnership Return, provided all partners fully report their shares of income, deductions, and credits on their timely-filed individual income tax returns (Form 1040).

Your business deductions will almost certainly include your automobile expense. You can deduct 20¢ per mile for the first 15,000 miles and 11¢ per mile for each mile thereafter driven in connection with your Amway distributorship. This mileage allowance is *in lieu* of deducting specific expense, e.g., gasoline, oil, insurance, tires, repairs, depreciation, etc. Your tax consultant can best determine which of the various methods of computing and deducting automobile expenses is best suited to your particular situation.

If you use a portion of your home *exclusively and regularly* as an office, then you may be able to deduct a portion of your household expenses. Bear in mind, however, that in the case of a residence, no part of which is used for business purposes, the only allowable deductions in most instances are those for real estate taxes, interest, and casualty loss. A taxpayer *may not deduct* any other expenses (such as depreciation) connected with the business use of his home unless they are attributable to the portion of the home used *exclusively and on a regular basis*, as:

(1) His principal place of business, or
(2) A place of business used by customers meeting or dealing with the taxpayers in the normal course of business.

CAUTION: The IRS has taken the position that a taxpayer can have only *one principal place of business* regardless of the number of business activities in which he is engaged. Under this narrow interpretation, a part-time distributor who earned more income from another business activity or as wages from employment may not be entitled to the home-office deductions discussed above if the home-office was used for his Amway business. Although the Tax Court has rejected this narrow interpretation in a recent case, its decision has been appealed by the IRS. For this reason, anyone considering deducting such expenses should consult his tax advisor.

Expenses which are properly allocable to a specific space within the taxpayer's dwelling which is used on a regular basis for storage of inventory held by the taxpayer for use in his trade or business of selling products at retail or wholesale *may be deductible.* However, in order to deduct expenses related to an inventory storage area, *the taxpayer's dwelling must be the only* fixed location of his trade or business.

Other business expenses that *may* be deductible or that *may* provide a credit under certain circumstances include:

- Child-care
- Depreciation of office equipment
- Purchase of new equipment (investment credit)
- Bad debts or refunds to customers
- Postage
- Seminar and meeting expenses
- Advertising
- Telephone and long-distance business calls
- Cost of sales aids, sales and product kits
- Accounting costs
- Stationery and printing
- Cost of gifts to customer (limit: $25 per year to customer)
- Contract labor paid to someone to assist you
- Legal expenses pertaining to your business
- Your "Notice of Intent to Continue Your Amway Distributorship" and Amagram/Literature update subscription
- Interest paid on business debts
- Office supplies
- Customer prospect entertainment (detailed records required)
- Hotels, meals, and lodging while away from home overnight on distributorship business
- Airline, rail, or bus transportation for business purposes

The deduction and credits listed above relate only to the major tax aspects of your Amway distributorship and your status as a self-employed person. Your tax consultant will assist you in determining other allowable deductions, such as medical expenses, charitable contributions, nonbusiness interest, nonbusiness taxes, and in determining capital gains and losses and other income.

Please share this information with the other distributors in your group.

January 7, 1982 NEWSGRAM/

SPECIAL BULLETIN

The time for preparing and filing income tax returns for calendar year 1981 is rapidly approaching.

The Internal Revenue Service is interested in alerting taxpayers about the impropriety of some deductions so that the taxpayer may be spared inconvenience and financial loss from claiming non-deductible expenses as "business expenses." The IRS is continually implementing new and more sophisticated testing methods to spot those returns which are selected for review. The IRS has asked that we publish the following information to alert you to the development of these new techniques and to caution you against claiming as business expenses those expenses which are actually of a personal character and, therefore, not deductible on Schedule C of your Form 1040 federal income tax return.

The information following, then, was prepared by the IRS and carefully reviewed by Amway's Legal and Tax Departments:

"WHAT ARE THE CHANCES OF AN IRS AUDIT?"
"NEW 'SELECTION TOOLS' IMPROVE CHANCES FOR SOME"

“Everyone knows the IRS cannot examine the tax returns of all taxpayers in the country. During fiscal year 1980, the agency examined less than 2 million individual returns. Over 93,000,000 returns were filed that year. That means that during 1980, your chance of being audited was about two percent, right? By no means, says IRS! What really counts is what's on your return, whether your return is among those in the agency's special compliance projects, and how high your 'DIF Score' is.

The IRS's basic method of identifying problem returns is through a computer process of assigning a numerical score, the 'DIF Score', to each return filed. The number is the sum of a series of weighted plus and minus values assigned to various entries on the form.

These weighted plus and minus values are developed through a program called TCMP, for Taxpayer Compliance Measurement Program. In this program, the IRS examines 50,000 returns selected through a statistically valid random sampling process. The returns are then examined in considerable detail. The statistical findings establish the norms for the various income groups and are used in the DIF scoring process. In a sense, your return is measured against a peer model. Deviations (or errors) appear as higher line-item values which in turn result in a higher DIF score.

Once all returns have been so scored, it's a simple matter to ask the computer to identify those with the highest scores — those most likely to be in need of audit. Before audits are scheduled, however, experienced technicians review the computer-selected returns.

Another way your return may be subjected to an IRS examination is through one of the IRS's many special compliance projects. These projects would include those employed in jobs which, based on IRS experience, are more likely to have understated income or overstated expenses.

IRS says its objective in selecting returns for examination is to avoid selecting a return that is basically correct and to flag the one likely to be in error. You can see, therefore, that percentages don't mean much when it comes to determining examination chances.

The agency believes it has been doing a pretty good job selecting the error-prone returns, pointing as an example to last year's results: 2.2 million individual, business, and other returns examined with $9.4 billion in additional taxes and penalties assessed. Despite these results, IRS continues to look for better ways of doing things..

Under DIF, IRS reduced its 'no change' examinations from 45 percent to 21 percent of those selected. Good results? Good, but not good enough, says IRS, so they have come up with a new, more efficient means of classifying returns for the DIF selection process. It's called TPI, for Total Positive Income. TPI is a different method of classifying returns into various classes of 'income'. TPI has been in effect since 1980. How is it doing? IRS is as pleased as a new parent. TPI, they say, is identifying problem returns which were overlooked in the past. Included among them are returns which show various kinds of losses that the agency feels are questionable.

During 1978, IRS conducted a study to determine if it could improve the method of using Adjusted Gross Income (AGI) to group individual returns into income classes. Income classes are used in DIF scoring, planning work-load and staffing, and monitoring results of examinations. The study group recommended new classes to group returns for better use of IRS examination resources. Total Positive Income (TPI) is the sum of all positive income values appearing on the return, such as wages, dividends, interest, rents, and other income items. Losses and other negative items are treated as zero when classifying nonbusiness returns. Total Gross Receipts (TGR) are used in classifying business returns. Wage-earner returns with small business schedules are now treated as non-business returns under TPI. Their chances of getting a higher DIF score are thereby increased significantly, IRS says. The new classifying processes began with the 1979 individual returns filed in 1980.

The DIF/TPI and Special Projects processes, IRS says, are already calling to the attention of their Examination Division people thousands of returns that the less sophisticated AGI classification process overlooked. Some of the issues, as IRS calls questionable items, being spotlighted now are the types of things that often appear on returns of people with part-time business activities.

They include, says IRS:

1. Wage-earners with business schedules showing small gross receipts and net business losses.

2. Returns with the principal income from wages (Form W-2 income) and deductions for substantial automobile expenses. The IRS suspects these may really be nondeductible commuting expenses, not business expenses as claimed.

3. Expenses for entertainment and travel claimed as business expenses which, upon examination, are often found to be unallowable personal or family expenses. IRS says Code Section 162 permits only *ordinary and necessary business* expenses to be claimed in this category and that Section 274 requires detailed records for such expenses. IRS agents look for verification of who was entertained, when and where, business relationship, how much business was conducted, how often was the person(s) entertained, and did business actually result. Similar questions are asked about travel expense deduction.

4. Offices in the home raise a big question mark in the selection process, says IRS. A new, tighter provision of the law, Section 280, says home use expenses can be claimed only if the office portion of the home is used '*regularly and exclusively*' for the business purpose. The tax people underscore both qualifications and say the average home, practically speaking, usually does not meet the 'regular and exclusive' test.

5. Failure to adjust cost of goods sold for amounts the agency has found to include substantial items for personal consumption. Agents say cost of products used for personal consumption are sometimes given different descriptions on the tax return, being called 'samples' or 'product research' expenses.

IRS says they encourage taxpayers to claim all expenses that are properly allowable under the law, but, says the agency, other taxpayers should not have to carry the burden of the taxpayers who claim deductions that the law never intended. They say DIF, Special Projects, and TPI have been shown to be excellent tools to help ensure this doesn't happen and that the overall tax burden is being shared more equitably. ”

Amway Corporation believes that Amway distributors, as taxpayers, are entitled to claim ALL business expenses which are properly allowable under the Internal Revenue Code. But Amway Corporation does NOT condone asserting deductions which are not allowable under the law, for example those which are "personal" in character rather than true business expenses. Amway distributors should NOT rely upon casual remarks made by self-appointed experts as to the deductibility of certain expenditures as business expenses. Amway distributors should be sure that they are receiving tax advice from COMPETENT tax advisors, preferably Certified Public Accountants and/or Tax Attorneys. Representations made by so-called "tax experts" at "tax seminars" should be checked with your personal tax advisor before being claimed as allowable deductions on your personal federal income tax return.

Each January or February, Amway publishes as a supplement to the NEWSGRAM a general, instructional article about income tax matters. Amway also emphasizes the need for ALL Amway distributors to account for their Amway income on their income tax returns. While Amway suggests certain expenses which can be deducted from your gross income, Amway cautions that the applicability of those expenses in your particular case should be checked with your personal income tax advisor.

If you have any questions concerning the material set forth in this article, please contact Amway's Legal or Tax Department. We would appreciate your fullest cooperation in complying with federal, state, and local income tax laws.

Chairman STARK. Thank you, Mr. Van Andel.

I gather that your company was aware of a problem of the tape before this hearing. How was that problem described to you and brought to your attention?

Mr. VAN ANDEL. Well, we first became aware of the tape that you refer to—I will call it the Field's tape even though we recognize that it was apparently made by someone else at a seminar he held. This tape was sent to us in the latter part of August 1980, I believe. We were asked to review the tape in response to a letter of inquiry, and it was reviewed in October.

Now, we get hundreds of tapes that we have to review so we can't review them all of course the same day they come in but we eventually did get to transcribe it and review it. We inquired in January 1981 of Mr. Fields who assured us that he had not produced a tape but that it had been produced by someone else and he did not know where it came from apparently and we did not know where it came from. But we began to get some information from various distributors that this tape was in circulation and we contacted these people independently, individually by letter or by telephone and told them that we reviewed this tape and it contained in our judgment improper information. That they should not use the tape and they should immediately withdraw it from circulation.

In March 1981, Mr. Fields was contacted by letter and telephone again. He advised us that he would request any people that he knew who had the tape to stop distribution of this tape because, of course, we did not know where it was and that he was not actually promoting or distributing the tape himself.

In May 1981, a followup letter was sent to Mr. Fields requesting written confirmation of his retraction and nonpromotion of the tape. In August of 1981 the file was closed due to a lack of response from Mr. Fields as well as no further complaints regarding tape promotion from anyone else.

In November 1981, a letter was received by Mr. Halliday, our general counsel, discussing the Fields' tape from someone and in December 1981 we put some material out with regard to our views that this tape was not proper. I would quote from that—

> You should know that Amway Corp. is somewhat familiar with the cassette tape presenting a talk given by Alan Fields who claims he is a former IRS agent in California. We have communicated with Mr. Fields in the past and have advised him that the tape is improper and should not be made available to the other Amway distributors. It is our understanding that circulation of the tape has been discontinued since we have heard no further reports of it being offered from the field.

Furthermore, in that same communication we said, "Promotion of Amway sales as a tax shelter is of great concern to us; we urge you to discontinue use of such tapes in any way."

Then in December 1981 a proposal flyer came to our attention. So in January 1982 we had a meeting of our top distributor leadership in which we addressed them on this issue and discussed in detail the problems with this kind of misinformation. That was followed by more specific bulletins. In March of 1981 we sent a special tape recording to our direct distributors in which we specifically discussed this kind of advice and told people they should not follow it. That has been followed by still further news bulletins. In other words, we have, as we have become aware of this, intensified our response which is our general way of doing this and we now think that the response from us has now been so intensive that, in our judgment, the problem probably no longer is a serious problem.

Chairman **Stark**. My colleague, Congressman Fowler, had suggested earlier to Mr. Egger, if you were not here when they testified, that they are beginning to see some indication of overdeduction, overclaiming or exuberant claiming of deductions in regard to not only people in direct selling but self-employed people in many fields.

Congressman Fowler suggested that perhaps the Internal Revenue Service might prepare a booklet. There are so many, I suppose, hundreds of thousands of direct sellers and self-employed?

Mr. **Van Andel**. Four million.

Chairman **Stark**. It might be worthwhile preparing a booklet which would quite clearly emphasize perhaps the legitimate areas for deductions and also point out very clearly those areas which the Service feels might be an overstatement of expenses. Do you think that would be a useful kind of aid for people who distribute your products?

Mr. **Van Andel**. Yes, sir. I think preparation of a booklet by the Internal Revenue Service could have a salutary effect. We, as I pointed out, also publish a booklet in the form of a bulletin which you have which follows along similar lines. Part of the difficulty, of course, is that the taxpayer, for all practical purposes, is forced to use a tax preparer or a tax consultant or someone of that nature to help him do his returns because the complexity of the law has put it beyond the capability of a great many average Americans. A tax law being that complex can be interpreted in different ways even by tax preparers who are doing their best to give the best advice.

There are ambiguities. When we tell people to go to a tax preparer we have no way of telling them which tax preparer to go to.

Chairman **Stark**. I was just going to ask that. I think we have some laws now relating to control over tax preparers. Without getting into endorsement of various ones I think there are perhaps some that are nationwide, some identified as subsidiaries of major national corporations and I think even perhaps some banks may be doing it. Have you ever considered listing, without seeming to recommend but some who you feel have a high standard of ethics to whom you might refer your distributors?

Mr. **Van Andel**. That is a good possibility. We have done something of that nature very recently. We have a new tape recording that we have received that has been prepared by Touche Ross discussing with Amway distributors how to prepare their returns. We think that Touche Ross is a responsible company and they have given proper advice and we advise people to listen to that recording.

Chairman **Stark**. I would like to have a copy.

Mr. **Van Andel**. We can get it for you.

Chairman **Stark**. Just for 1 minute more. I am sure my colleagues would like to inquire. We await the Internal Revenue Service's results of their studies but if we find that people are overdeducting or overstating tax credits available to them, how do you view the idea that was proposed earlier of not reporting the first few hundreds of gross sales or just reporting it for informational purposes? We would presume that somebody getting started in the business has at least that many expenses anyway but go on to say that unless they get to some reasonable level of sales or revenue that they ought not to be able to deduct expenses attributable to that activity. Would that impact on the profitability of your legitimate representatives? When I say legitimate, those who are in business to make a profit selling products and not in business solely for tax deductions?

Mr. **Van Andel**. We think they are all legitimate. But I have not heard that proposal before. I do find it very interesting and I would want to think it through. The reason I say that is because the direct selling industry is made up of a number of different firms which operate in somewhat different fashions. Avon does not operate the same as we do, nor does Tupperware. Shakley is somewhat the same as we are. On the other hand, Mary Kay is a little different and so on. Each of these might respond to that in a little different way but I would think if that proposal were properly discussed in the forum of direct sellers, we would be able to come up with an answer to that.

Chairman **Stark**. It would be very helpful. I know we on the subcommittee and our staff may try to think of ways that we might extend the hobby farm concept to some direct sellers and I think that by weeding out the bad apples, as it were, it will allow your industry to continue to prosper and give people a chance to participate in the free enterprise system.

I would appreciate any suggestions you or your company might like to offer.

Mr. Vander Jagt.

Mr. **Vander Jagt**. Thank you very much, Mr. Chairman. I would like to thank you for what I think was an excellent statement. You did have an amazing story to tell. It is an amazing record through the Newsgram and the Amagram and the special bulletins of the extraordinary steps that Amway has taken over the years to assure compliance with the tax laws. I think it is a fine record and I am very happy that you were here to present the story. Thank you very much.

Chairman **Stark**. Mr. Fowler.

Mr. **Fowler**. Mr. Van Andel, also I want to thank you for your testimony and also say that just as one member I completely agree with your comments about complexity of the Tax Code. The burden is not only placed on taxpaying Americans but unless we do make some substantial changes in simplifying the Tax Code then we are going to run tremendous risk of noncompliance by the most well-meaning Americans who go the second, third and fourth miles to try to make sure that they are complying with not only the spirit but the letter of the law.

If you will allow me to ask you a couple of questions off of the subject, I suppose, but if the chairman will indulge me I would be very interested in talking to you a little bit about Amway's political activities.

There is no question that with 1 million distributors that go door-to-door, basically, that that could be a tremendous political organization which would certainly be your right under our free society.

I note that your partner and cofounder, Mr. DeVos is the chairman of the Republican National Finance Committee. That your ads seem to be more and more political in the newspapers, large ads, and I just wondered if you would share with us your thoughts as to the proper extent of political activity by an institution the size of Amway and what efforts you try to make through all of these publications and advice to your distributors as to what are the lines of business and the promotion of business and what is your advice on the promotion of yours and Mr. Devos' political theories?

Mr. VAN ANDEL. The Amway distributor organization is probably the largest volunteer army in the world, but I emphasize, volunteers. No one has to be an Amway distributor if they don't want to and anyone who is can quit instantaneously if they wish.

Therefore, it does not behoove us as leaders of that kind of organization to involve ourselves in those activities which would be devisive to such an organization. Obviously, not all Amway distributors are Republicans. They are not all Democrats. They are not all Independents. They are not all black or white or red or yellow. They are not all Catholic or Protestant. There is a total mixture across the board just as there is of all Americans.

Therefore, we have never made it a practice to involve ourselves in matters that have to do with religious convictions, outside of general moral principles, but not specific theological situations, nor issues that have to do with specific political matters as far as Amway Corp. itself is concerned.

We do believe that as a corporation, we can and should spend some of our resources to attempt to preserve the free American way of life, free enterprise, if you want to call it that, because a system such as ours, a business such as ours, obviously could not operate in the Soviet Union. It could not operate in mainland China or other nations of that type and therefore we think it behooves us to talk to our distributors about the free enterprise system and about the threats that may exist as we see them to the system in that framework only but in a nonpolitical framework.

Now, even there, when we talk about those issues, especially to the general public with regard to so-called advocacy advertising, as you may know, much of that kind of advertising is a nondeductible business expense. That has to be looked at, of course, on a case-by-case basis by the lawyers involved.

We do believe, however, that as individual Americans, my partner and I just as well as our employees, have every right to be involved in the personal advocacy of political positions or religious positions or whatever else we want to do in this country of free speech.

Mr. FOWLER. Absolutely.

Mr. VAN ANDEL. We have to be very careful, of course, that we do this as individuals on an individual platform and not on a corporate platform. Therefore, you might see me or my partner in a forum making a political speech to Americans but you will never see us on an Amway platform making such a speech. That would be a completely separate situation and we are very careful to keep those separate.

Mr. **Fowler**. Do you now publish or do you plan to publish, separately from your Newsgrams and Amagrams, any political advocacy over your signature and that of your partners?

Mr. **Van Andel**. We published advocacy advertising in national newspapers.

Mr. **Fowler**. I know that. I have seen that.

I mean, specific endorsement of candidates or advocating partisan politics, either Republican or Democratic. Do you plan, as we have elections approaching this year and national elections in 1984, to publish over your signatures and distribute, mail to your million distributors, personal political advocacy, admittedly separate from your Amway information?

Mr. **Van Andel**. No, we do not use that mailing list for that purpose.

Mr. **Fowler**. Do you allow the National Republican Party to use it for any purpose?

Mr. **Van Andel**. No one uses that mailing list for any purpose. That mailing list is totally restricted.

We could sell it many times over, I'm sure, if we wished. We do, of course, have a corporate PAC. Mr. Gartland, sitting here, manages that PAC and operates it according to the law.

Mr. **Fowler**. I have never had the pleasure of seeing it, Mr. Gartland.

I appreciate those responses, Mr. Van Andel, and I anticipated them. I appreciate not only what you are trying to do but I hope that you have the right, of course, to make the choices as you indicated, of your own politics, but I know you also got a good battery of lawyers to make sure that you try to keep those two separate just for the obvious troubles that we could incur with an organization of your size.

Just a couple of quick questions, Mr. Chairman.

In your statement on page 6, back to the issue at hand, in the last paragraph you were talking about if problems with the tape and problems with Amway distributors, how you attempt to resolve these and are able to resolve these usually by working with the people involved, can you tell me how many distributors last year, the year before, for whatever reason you have had to terminate?

Mr. **Van Andel**. I don't think I could answer the question but perhaps I could elucidate on your question a bit in this way. We have a disciplinary system which is three steps; three tier. It starts with counseling. Counseling is done by mail, by telephone or in person. Obviously the first thing to do is to try to get people straightened out on that basis if they will straighten up.

The second step, if counseling does not work is to move into what we call censure. Now, censure freezes the activity in a distributorship and requires the distributorship to go through a retraining period. While under censure, they are not authorized to add to their business by sponsoring new distributors and so forth. After censure they are, of course, given a period of time to show us that they now are operating in a proper fashion and if that doesn't take, then the final step is termination.

Mr. **Fowler**. What are the usual difficulties that would lead you to initiate the process of discipline with a distributor? What are the usual difficulties distributors get into?

Mr. **Van Andel.** Well, one of the difficulties has been recently presenting the business as a tax shelter. We have censured and terminated people for that reason. There may be other forms of misrepresentation. Misrepresentation may take place with regard to misrepresenting the business itself or misrepresentation of products. Most of our products that we sell today come under the regulatory aegis of one or various regulatory agencies. The Food and Drug Administration, as an example, for our food supplement products. If we have a distributor that refuses to comply with the regulations of the Food and Drug Administration, then that would be misrepresentation and we would have to ultimately follow through those steps. It is that kind of thing.

Mr. **Fowler.** One final question, Mr. Chairman.

Mr. Van Andel, when at the beginning of your testifying about the Fields tape and the reasons for your immediate action through all of your network to put that tape out of circulation, is it a fair statement by me to say that when you and your lawyers heard that Fields tape it was immediately obvious that Mr. Fields was advocating tax information that simply was false?

Mr. **Van Andel.** I think that's what the conclusion of our lawyers was, yes, sir.

Chairman **Stark.** Mr. Van Andel, I just have one more question and I am darned if I can remember the exact format of the ad. Generally, I give your advertising agency good marks. As I recall, it was a man driving a car with someone in the car. It was a nice new car and the passenger was asking where he got it. The implication of the ad was that he had become an Amway distributor or seller and it provided additional income.

It was, in effect, I would assume, an ad to encourage people to find out about the advantages of becoming associated with your company. I think perhaps it had an 800 phone number.

I don't recall that there was anything in there that indicated that Uncle Sam was taking too much of your tax dollar or it is too hard to get ahead today with all the taxes we are paying, but would you feel that that is a good way to recruit or that that kind of reference ought to be left out of your recruiting advertising?

Maybe not. Because there are obviously some expenses that are legitimate and deductible. I can't recall whether I saw it in that ad. I guess it was hinting at some of the advantages that are available. I would imagine that they would be available legitimately.

Mr. **Van Andel.** Let me just quote from various letters and bulletins that we have sent to distributors on that particular question.

Let me first state that the Amway sales and marketing plan is not a tax shelter. Moreover, any tax consequences that result from the operation of an Amway distributorship are not much different than the tax consequences that result from the operation of any small business. In other words, the income from an Amway distributorship is taxable gross income and the ordinary and necessary business expenses incurred in the operation of the distributorship are deductible.

The letter goes on to say, accordingly, Amway Corp. does not in any way describe the Amway sales and marketing plan as a tax shelter. Accordingly, Amway Corp. produces absolutely no literature which promotes any tax benefits of becoming an Amway distributor because it is not at all clear that there are any.

Chairman **Stark**. I think there may be some but I am not sure that that's the best reason to enter into it.

Mr. **Van Andel**. That's not the best reason. We promote the business for what it is, a business of earning income.

Chairman **Stark**. I want to thank you very much for taking the time from your busy schedule to testify. I look forward to getting a copy of that tape and to getting your suggestions or suggestions from your industry as to what we might do, if anything, to see that we have voluntary compliance by the members participating in your industry.

Thank you very much.

Mr. **Van Andel**. Thank you.

Chairman **Stark**. Our next witness is Mr. Neil Offen, president of the Direct Selling Association, who is accompanied by Mr. Arthur J. Rothkopf of Hogan & Hartson, and John C. Beyer, president of Robert R. Nathan Associates.

Mr. Offen, welcome. I notice that you do not have a prepared statement, so we will take very careful note of every word you utter and welcome you to the committee today.

STATEMENT OF NEIL OFFEN, PRESIDENT, DIRECT SELLING ASSOCIATION, ACCOMPANIED BY ARTHUR J. ROTHKOPF, HOGAN & HARTSON, AND JOHN C. BEYER, PRESIDENT, ROBERT R. NATHAN ASSOCIATES

Mr. **Offen**. Thank you very much, Mr. Chairman.

On my left, Mr. Rothkopf, who serves as tax counsel to the association, and on my right is Mr. John Beyer, president of Robert R. Nathan Associates, our consulting economist.

Since we did not know quite what would be relevant to discuss today, we did not prepare a formal submission. But I do have some notes that I would like to refer to and go through briefly.

Specifically, I would like to first describe the Direct Selling Association for those of you who may not be familiar with it. It now consists of 105 corporations which deal through approximately 4 to 5 million independent contractor sales people. Direct selling is really not an industry. It is a method of distribution.

It has high ticket companies, low ticket companies, multilevel companies, door-to-door companies, route sales, direct mail combinations with direct selling, various other uses of the telephone for sales purposes as well as deposit commission operations.

So it is an entire method of distribution.

Chairman **Stark**. What is the deposit commission operation?

Mr. **Offen**. Deposit commission types of operations are where there is a sales person who will take a deposit from the consumer and that deposit will be the remuneration for the individual sales person. The corporation with whom that sales person deals never sends any form of compensation to the individual. But it is not a situation where that sales person purchases the product from the corporation, but rather is on a remuneration system that consists of the deposit.

We do about $7.5 billion a year or at least in 1980 that was our retail sales volume for the industry in the United States to the best of our estimate. Women are 80 percent of our sales people; 15 percent are minority group members; 10 percent have some sort of physical disability, often temporary, not permanent; and an additional 200,000-plus are over 65 years of age.

The barriers to income earning opportunity traditionally found in our society are not found in direct selling. This is largely due to the very nature of the independent contractor relationship that the sales people have to the corporations. There is no incremental cost to speak of to add someone to the sales organization.

Lou Harris, in a study he did for us recently, indicated that during the course of 1 year, 8 percent of the homes in this country will have someone living in those homes who sells for one of our firms. An additional 15 percent of all households in this country have someone who, in the past has sold for one of our member firms or nonmember firms in the industry.

In other words, almost a full one-quarter of all households in this country will have this year or have had in the past someone living in that household who has been a direct seller.

We have been dealing with the IRS about the independent contractor issue for 12 years. It is a little bit ironic to see where we are today at this hearing, since 12 years ago the issue was whether or not these people were employees of corporations or independent small business people.

The IRS, attempting to reclassify these people, indicated that they were employees. The IRS contended that you needed a major capital investment to be an independent contractor and it violated other common law principles that apply as well. This resulted in Congress taking action against the Service, forbidding the Service from doing reclassifications until Congress comes up with a solution to the independent contractor issue, which this subcommittee is charged with.

We hope to be here before you again to talk about that issue at hearing on the subject.

The issue of the controversy then went to the second stage which went from the classification issue to the allegation that direct sellers and other independent contractors were not filing their tax returns, not paying their taxes. Well, that issue has now been addressed by Robert R. Nathan Associates, and numerous other economists and consultants to the other independent contractor groups, and we think has been effectively rebutted.

Now today we are faced with a 180 degree turn where we are seeing an allegation that is being made that not only are people filing returns but they are overstating the deductions. So we go from a situation where we are dealing with the allegation that they were not filing their returns, to an allegation that not only are they filing but they are taking sophisticated tax shelters as a result.

We respectfully but strongly object to any suggestion that direct sales people present special compliance problems in respect to claiming excessive deductions. Such a suggestion, we fear, improperly casts doubt on the integrity of millions of law abiding taxpayers or independent business people engaged in direct selling.

The question of whether self-employed individuals are claiming more tax deductions than those to which they are entitled is a broad ranging issue that extends far beyond direct selling.

The American economy has within it hundreds of professions and occupations in which self-employed individuals such as lawyers, accountants, doctors, architects, real estate brokers, cab drivers, insurance salesmen, construction contractors, loggers, truckers, freelance writers, management consultants, and others, including some lobbyists, are claiming tax deductions for expenses incurred in the courses of their professions or occupations.

We fail to comprehend why of all these many occupations, those engaged in direct selling are the subject of a special study that does not purport to be representative of all direct sellers or of all self-employed individuals. Indeed we have no reason to believe, nor have we seen any credible evidence to suggest that direct sellers prevent any greater compliance problem in the area of excessive deductions than other self-employed individuals. In fact, the Joint Committee today stated that the examples are not from a valid statistical sample of returns.

We fully recognize that there are many individuals engaged in direct selling as well as in other occupations who might overstate their legitimate tax deductions. We disown such activities and urge the IRS to develop appropriate compliance techniques to prevent this.

It should be pointed out that DSA has consistently supported efforts to obtain increased funding for the IRS in order to achieve higher levels of taxpayer compliance. In addition, your suggestion of a pamphlet to be developed by the IRS strikes us as a good one.

The direct selling industry has had a long history of cooperation with the Internal Revenue Service to encourage voluntary compliance on the part of direct selling companies and their sales people. Over the past 10 years, many meetings have been held with IRS personnel, almost invariably at the insistance of DSA, to determine additional ways in which compliance levels of those engaged in direct selling could be improved.

These efforts on the part of the industry have not gone unnoticed as reflected in the letter received by an attorney representing a major direct selling company dated October 17, 1977, from the office of the Commissioner of Internal Revenue Service, which acknowledged, "A history of concern and cooperation on the part of the Direct Selling Association with the Internal Revenue Service in our cooperative efforts to promote voluntary compliance."

These efforts, over a period of many years have borne fruit in an extensive educational program engaged in by direct selling companies to assist and encourage their sales people to fully and accurately report their income and deductions attributable to direct selling.

DSA's member companies have an excellent record of distributing to their sales people detailed information on a frequent basis that explains to the sales people their Federal income and employment tax responsibilities. This written material demonstrates a real concern on the part of the companies for tax compliance which we believe is reflected in an excellent compliance record on the part of those engaged in direct selling.

I would finally like to respond to some of the other points raised here today. We would like to know who was selected for audit. Mr. McConaghy indicated that there were quote many unquote, direct selling companies. As best we can determine, there were maybe one or two.

I would like to see a response to that, Mr. Chairman. In addition, we are a little skeptical of IRS studies since, in the independent contractor study in terms of their definition of direct sellers, we found an awful lot of people who did not belong in that classification.

For example, 10 percent of those included as direct sellers were listed as entertainers, which the IRS subsequently admitted was an error. In addition, there were people listed as manual laborers. We do not know who those people are.

Finally, not one of the members of our association, to the best of our knowledge, had any of their sales people included in that former IRS study. So we are a little IRS study shy.

In addition, we would like to learn about people who have overpaid their taxes by not claiming all their deductions. We suspect that there are a lot of people out there, and that is one of the reasons why we are trying to educate our people not only as to their tax obligations but their right to take legitimate, valid deductions.

A lot of people may be overpaying their taxes rather than overstating their deductions.

Finally, the concept of withholding was raised by Commissioner Egger. We think withholding which is totally unacceptable to our industry as a solution to the independent contractor issue, is not relevent to this issue at all. I do not see why the Commissioner brought up withholding in terms of this potential problem.

We would finally call your attention to the bill introduced as a bipartisan measure by Senator Dole, S. 2369, which we hope to see introduced by members on both sides of the aisle of the Ways and Means Committee. S. 2369 deals with some new information reporting burdens on direct sellers that we have accepted in the hope of showing good faith and in an attempt to approve compliance. We are urging it be tied to a safe harbor that can be defined by this committee and reported to the full committee and to the floor of the House and enacted this year prior to the expiration of the prohibition on IRS taking more reclassification steps.

Thank you, Mr. Chairman.

Chairman STARK. Thank you.

Mr. Vander Jagt.

Mr. VANDER JAGT. Mr. Chairman, I appreciate very much your graciousness in letting me go first because of a prior commitment. I wanted this opportunity to welcome Neil Offen to the Ways and Means Committee, and to thank him for a very fine statement.

I think you have raised some very good questions and the chairman has assured me that the record will be kept open for 5 days so that members who where not here would be able to submit questions to some of the witnesses.

Chairman STARK. Without objection.

Mr. VANDER JAGT. Thank you, Mr. Chairman.

So maybe we will be able to get some answers to some of the questions that you have raised.

Thank you very much.

Chairman **Stark**. Thank you, Neil. Let me see if I can address some of your concerns.

I share with you your concern about withholding and its applicability to all the companies in your industry. I want to assure you that direct sellers, as distinct from self-employed people, were not intended to be singled out in this hearing. I am sure you know the history of how this came to my attention.

We have been looking at this issue ever since I have been a member of this committee. We have been talking about independent contractors and/or self-employed people from the whole standpoint of income reporting, and the issue of zealous deductions or overdeductions or overstatement of deductions never came up.

I did, as a result of the approach that was made to me, talk with people that I know in the Internal Revenue Service.

And I learned for the first time a couple of months ago that there indeed is a problem. I would phrase it to various district directors I talked to and said, what is the problem? And they said, "If there is any problem, it is one that is building and it is one of overdeducting, or claiming more deductions than those to which people are entitled."

So under the rotten apple theory, which is probably why we knocked out hobby farms some years ago, I suspect we are finding a few, and the Fields case is a perfect example of something I think everybody agrees should not be done. It was probably used in an attempt to recruit.

I do not know what the benefits of recruiting somebody are as opposed to selling, but it is obvious people were pitching, and I hate to use the word tax dodge, but I think that becomes apparent to anybody hearing the pitch, that it was far more a tax dodge than it was a legitimate approach to encourage somebody to sell a product.

I would look with you for some ways to limit that. As we talked earlier, when I talked to Mr. Van Andel, it might be only one end of the spectrum where there is a high incidence of turnover in low ticket item sales people. I think there may be a high incidence of those people who have very limited gross sales.

It might be the better part of valor from the standpoint of the IRS and your industry to do something like limiting the amount that is actually included in income, while restricting deductions. If you assume they are going to have that many expenses in getting started, if they get to some level and want to itemize, perhaps they should.

But I think that the IRS has followed its investigation more through tax preparers than a particular industry. So that if there happened to be certain areas where tax preparers are flourishing and are doing this, I think maybe the problem may be that we have to be tougher with tax preparers.

But I do not want you to get the feeling that it is something that applies only to direct sellers. It may apply to self-employed people, and to small businesses. I do not know that. But I was unaware that there was such an extensive investigation going on.

As you well know, a month or so ago we postponed the independent contractor hearings at the request of the Treasury. They had also stumbled on this problem and felt that it ought perhaps to be discussed in light of Senator Dole's concern, and Congressman Conable's concern with the underground economy whether or not it properly fits in the independent contractor bill.

If legislation is needed, and I am not at all sure that is the case, maybe more agents are needed to enforce present laws or regulations, or maybe we need some different regulations, I am sure your industry would, as they have in the past, be very responsible and help us by contributing to find a way to solve the problem rather than be an adversary.

So I certainly do not want you to feel that your industry is being picked on. It is unfortunate that the tape that came to light was used primarily by one company. The question I addressed to Mr. McConaghy, was for the sole purpose of identifying that this was not only Amway. I think there were perhaps two or three other companies in the small number of returns Mark reviewed, and I asked that question to establish the fact that this was not entirely an Amway problem.

That is the only reason.

Mr. OFFEN. Then his response that there were many would not be accurate?

Chairman STARK. Several would be more accurate. I have not seen the returns.

Mr. OFFEN. Of the 1981 returns, what about the 61 that were not submitted as case studies? There were 61 returns that were apparently audited. What about the other 61 that were not part of the case studies?

Were those found to be people who had not overstated deductions?

Chairman STARK. To be perfectly honest with you, the only ones I have seen were the ones that were in the statement. I would be glad to find out what was in the others. I am told they were all approximately the same, all 80, and that the 20 were chosen as representatives of the rest.

I am sure that if they are in sanitized form, if you or any people of your staff would like to look through them, I am sure I could arrange to get copies.

Mr. OFFEN. I think it would be useful also, if it is possible, to see what the breakdown was of how many people were affiliated with one or two companies specifically. Is it 90 percent with one company and the remainder——

Chairman STARK. My guess would be that that is probably the case.

Mr. OFFEN. The reason I am asking the question is that this is a new issue for us. We have never heard this allegation before until Commissioner Egger——

Chairman STARK. I can assure you, Mr. Offen, it is new for me and the staff of this subcommittee. As I say, it is coincidental, believe me, that this came up. I think that it is one that we ought to address.

I suspect it is far, far broader in the whole concept of—what I think Senator Dole is concerned about. I think there are a lot of people out in the world who think it is, and the only word I can think of, it is the smart aleck approach.

It is the cocktail party conversation that probably was describing the condominium home when there was no depreciation. Now I suspect there is a feeling abroad in the land that if you are paying very much in the way of income taxes, that you are a sucker.

I don't ascribe any of that to your association. It may be that the major Fortune 500 companies are getting us to do that because publicly they can be identified as not paying any tax and the attitude is well, if the rich guys aren't paying any, how come I am?

I think it is very important to our tax system that we make very clear that there are very specific rules about what you can deduct and why, and that casual promotion, as Amway mentions in their literature, of tax deductions is something we shouldn't condone.

I don't know as you and I have any disagreement on what the problem might be. I think perhaps working together we can find a solution.

Mr. **Offen**. We don't disagree with the objectives that this committee has espoused. It doesn't follow, though, with our profiles that we have had done on our salespeople that they would be the type of people who would be using those types of tax shelter frauds.

We will be submitting to your staff various examples of the educational materials that the companies do, as well as a study done by Lou Harris as to the nature of our sales people, almost a profile of them.

[The following was subsequently received:]

Supplement to Newsgram
April 22 1982

AMWAY IS NOT A TAX SHELTER! IMPORTANT READING FOR ALL AMWAY DISTRIBUTORS

Over recent months, Amway has become increasingly concerned about a new form of distortion of the Amway Sales and Marketing Plan. We are referring to the representation of the Amway Sales and Marketing Plan as a "tax shelter", which it most assuredly is *not*. An Amway distributorship is a profit-making venture. Like the profits from any legitimate business enterprise, the profits of an Amway distributorship will be taxed.

Nevertheless, a misguided few have begun to promote the Plan as a vehicle by which an individual can claim extraordinary "tax deductions", thereby leaving himself in a "zero profit" or even a "tax loss" situation. These misguided few assert that, as a result of becoming an Amway distributor, an individual will thus have to pay no taxes on their Amway income and may even be able to "save taxes" on that non-Amway income because of the "tax loss" from their Amway distributorship.

Amway will not tolerate this distortion of the Plan. With this in mind, it is our duty to bring to your attention seven of the most outlandish such distortions, which, unfortunately, have received somewhat wide dissemination.

THE MYTH	THE REALITY
1. **"Virtually WRITE OFF the Highest Proportion of Your Personal Expenses!"**	1. Without delving into the technical complexities of the Internal Revenue Code, it is extremely doubtful whether an Amway distributor can write off **any** of his "personal expenses". Accordingly, to suggest that by becoming an Amway distributor, one can "Virtually **Write Off the Highest Proportion of Your Personal Expenses**" is absurd. There simply is no magic sword that comes down on the shoulder of a new Amway distributor and somehow converts his nondeductible personal expenses to business deductions.
2. **"Add $10,000.00 to Your Income This Year and NOT PAY ANY TAXES On It!"**	2. The only way an individual could add $10,000 to his income and not pay any taxes on it is if he had $10,000 of gross income and another $10,000 of legitimate business deductions. A distributor with $10,000 of gross income would normally be expected to have considerably less than $10,000 of legitimate business deductions, with the consequence that taxes **will be due** on the resulting profits.
3. **"Get Back Part of What You Are Paying on Your Present Income!"**	3. The statement that you will "**Get Back Part of What You Are Paying on Your Present Income**" is made with the expectation that an individual will have so much of a "tax loss" from his or her Amway distributorship that that "tax loss" will reduce the amount of taxes owed on income from present sources. Since a distributorship will rarely have a legitimate tax loss for any sustained period, this statement has no validity.

4. "**WRITE OFF** Most of Your **Telephone. Home Expenses. Depreciation** and **Auto Expenses Including the Cost of Commuting to Work!**"	4. There is no way a distributor will legitimately be able to deduct "Most" of his or her telephone, home expenses, and auto expenses. Depreciation on one's personal residence will be permitted only to the extent (assuming other conditions are met) that that personal residence is used regularly and exclusively in connection with the distributorship. **Any personal use whatsoever** of a dining room, living room, etc. will result in that portion of your home **not** being depreciable at all. Lastly, commuting is **never deductible**. Operating a distributorship in your home either before you leave for work in the morning or after you return from work at night will not result in your nondeductible commuting being converted into deductible commuting.
5. "**ALL PRODUCTS USED IN YOUR HOME** the First Year are **DEDUCTIBLE!**"	5. One of the most ridiculous myths relates to the "personal use deduction". The cost of products consumed in demonstrations is deductible. The cost of products given away as samples to bona fide customers or bona fide prospective customers is deductible. The cost of products personally consumed is **not** deductible. Thus, to suggest that "**ALL PRODUCTS USED IN YOUR HOME** the First Year are **DEDUCTIBLE**" is ridiculous because the cost of **none** of the products taken from your inventory for personal consumption is deductible.
6. "**BUY AT WHOLESALE FOR YOUR PERSONAL USE!** Over 300 Consumable Products and the '**Amway PERSONAL SHOPPERS CATALOG**' **has Over 4,000 Items** Ranging from Microwave Ovens, T.V.'s, Stereos, Video Recorders, Cameras, Clothes, Tools, Toys and Much, Much More . . . and **JUST THINK OF IT . . . THEY'RE ALL TAX DEDUCTIBLE!!!**"	6. The representation that all of the products bought from the Amway Personal Shoppers Catalog are "**ALL TAX-DEDUCTIBLE**" is a variation of the "personal use deduction" myth. No part of the cost of products bought from the Amway Personal Shoppers Catalog which are used primarily for personal purposes is deductible. For example, the television in your family room, the microwave oven in your kitchen, and the grandfather clock in your hallway will necessarily and correctly be viewed by the IRS as being primarily used for personal purposes and will thus **not be deductible.**
7. "**WRITE OFF** Entertainment & Travel Including Vacation Trips Abroad!"	7. These statements are **false**. They are **myths**. An Internal Revenue Service auditor reviewing the tax return of any distributor who follows this "advice" will disallow the unwarranted deductions. Moreover, a distributor claiming these kinds of deductions is not only deceiving himself, but, if that distributor also encourages another individual to become an Amway distributor on the basis of these misrepresentations, that sponsoring distributor has **badly** misled his prospect. The only way travel expense can be deductible is if the **primary** purpose of the trip is business as opposed to personal. That determination is made upon the basis of all the facts and circumstances surrounding the trip, the most important of which is usually the amount of time spent on business as opposed to personal pursuits. A vacation is obviously a personal pursuit. Thus, to suggest that anyone can write off the costs of vacation trips, whether at home or abroad, is **false**.

Occasionally, an advertisement for a "tax shelter" will include the name of a prominent Amway distributor. In most cases, the distributor's name was used without their knowledge and does not constitute an endorsement of any kind.

We hope that this information will help set the record straight regarding the distortions of the Amway Sales and Marketing Plan. Amway Corporation and Amway distributors will continue to grow and prosper. That growth and prosperity will be done by promoting the Amway Sales and Marketing Plan as the outstanding business opportunity that it is. It will not be done through distortions of the plan which leave one to believe that, by becoming an Amway distributor, one can ignore, avoid, or otherwise circumvent the tax laws. Such distortions do a disservice to those who make them and do an even greater disservice by misleading the individual who may believe them.

DC-143

THE TAX ASPECTS OF YOUR MARY KAY CAREER

As a Mary Kay Consultant, you are considered a self-employed person and may be entitled to special tax deductions. Generally, it is preferable to have a CPA or tax accountant prepare your return for you. The cost is usually small when compared to the savings which may be accomplished. You should spend some time with the preparer to ensure that he fully understands your method of doing business and your status as a self-employed person. This enables him to claim deductions for you which otherwise might not be evident to him. However, if you prepare your own return, you can obtain at modest cost, various booklets explaining income tax laws from any Internal Revenue Service office and most post offices. The most important thing in preparing your tax return and assuring that you have the benefit of all proper deductions, are adequate records of all income and expenses. Such records are essential in the preparation of the return and substantiation of income and expenses if your return is examined by the Internal Revenue Service.

Income and expenses incurred in your Mary Kay career are normally reported on a special tax form, Schedule C, which is provided by the Internal Revenue Service. This form is designed especially for self-employed persons. Following are points that should be considered in calculating your net income for tax purposes.

(1) GROSS RECEIPTS: The calculation of the gross receipts made during the year is the first step in preparing your income tax return. To retail sales, you must add any recruiter and sales director commissions received and the fair market value of company promotions and awards received during the year. Commissions and the fair market value of promotions and awards are reported to you and to the Internal Revenue Service each year by the Company. The total of these items comprise gross receipts, from which all costs and business expenses are deducted. Be sure that in the calculation of gross receipts, sales taxes, hostess credits and charge card discounts are not deducted more than once. For example, if retail sales are reported after the allowance of the hostess credit, it cannot be deducted again as a business expense.

(2) COST OF GOODS SOLD: The first deduction from gross receipts is the cost of merchandise that you have sold during the year. The calculation of your merchandise cost is demonstrated as follows.

ADD	Wholesale value of inventory at beginning of year.
PLUS:	Wholesale value of purchases during the year.
LESS	Wholesale value of inventory at end of the year.
EQUALS:	Cost of goods sold during the year.

In the calculations above, it is necessary that you determine the wholesale value of your inventory of goods on-hand at the beginning and at the end of each year. This is easily done by listing merchandise on-hand on a Consultant Order Sheet as you would a regular order. If the inventory is counted a few days after year end, merely add to the total, the wholesale value of merchandise sold, based on information from sales tickets dated after year end.

(3) AUTOMOBILE EXPENSES: Business related automobile expenses may be deducted in one of two ways. Individuals can deduct a standard mileage allowance or use the allocation method to determine the deduction. Also, gasoline taxes attributable to non-business use, parking fees, tolls and investment tax credits are deductible in addition to the standard mileage allowance. However, this method may not be used where accelerated depreciation or additional first year depreciation has been claimed.

The standard mileage allowance changes periodically with current rates included in forms and instructions received by taxpayers from the Internal Revenue Service.

In the allocation method, a fraction is determined, the numerator of which is the total business miles driven during the year and the denominator is the total business and non-business miles driven during the year. Once determined, this fraction is applied to all expenses of operating the automobile, such as gas, oil, repairs, licenses, insurance and depreciation. Interest on car loans and taxes are includable with automobile expenses for the purpose of determining the allowable business expense. The portion of these expenses that is not claimed as a business expense may be deducted as an itemized deduction.

(4) TRAVEL EXPENSES: Travel expenses which include meals, lodging and necessary incidental costs, are deductible while the taxpayer is away from home in the pursuit of a trade or business. The expenses must be ordinary and reasonable in amount under the circumstances. As long as the purpose of the trip is primarily for business reasons, travel expenses are deductible even though the taxpayer may spend some time in sightseeing, visiting, entertaining, etc. Such expenses, however, are not deductible if the trip is primarily personal in nature. A spouse's travel expenses are not deductible unless the spouse's presence on the trip has a business purpose.

(5) ENTERTAINMENT EXPENSES: Generally, entertainment expenses are deductible if they are ordinary and necessary to the taxpayer's business. Expenses for entertainment for the purpose of generating goodwill are normally deductible if there is a good possibility of the entertainment producing future income. However, no deduction is allowed for entertainment expenses to the extent that they are extravagant in the circumstances. Business meals can be deducted if they are held in surroundings

conducive to the business discussion. In the area of entertainment expenses, documentation of the business purpose is generally necessary. This would include the name and relationship of the person entertained and the items of business discussed during the entertainment.

(6) OFFICE AT HOME EXPENSES: The office at home deduction is available only where a specific portion of the home is used exclusively and on a regular basis, as the taxpayer's principle place of business or used by the taxpayer for meetings or dealings with customers. This requirement is not met if the portion is used for both business and personal purposes. The deduction is limited to the gross income generated from the use of the residence, reduced by an expenditure that would otherwise be deductible such as taxes and interest. Deductions are allowed for items allocable to space in the home regularly used for inventory storage.

(7) CHILD CARE CREDIT: Individuals are entitled to a tax credit for qualifying child care expenses. Household and personal care expenses for a dependent under fifteen, or a spouse, or a dependent incapable of self-care, qualify if incurred in order to allow the taxpayer to earn income. The credit is available to working married couples or couples where one works full-time and the other works part-time or is a full-time student. The qualifying expenses are limited to the earnings of the spouse with the lower income. Credit is also available to a working divorced or separated parent if he or she has custody of the child under fifteen.

(8) OTHER. As a self-employed person, you are subject to self-employment tax which is assessed in lieu of social security tax. The rate, form and instructions are included with your return. In addition, if you exceed certain income minimums, you are required to file a declaration of estimated income tax and pay quarterly installments of such estimated tax. You should investigate the requirement carefully to determine whether it applies to your situation. Instructions for filing and paying estimated taxes are included in your return. Before filing your return, you should consider the tax implications of other income and expenses such as medical expenses, charitable contributions, other itemized deductions, capital gains or losses, miscellaneous income, etc.

AS TAX LAWS AND REGULATIONS ARE CONSTANTLY BEING AMENDED OR CHANGED, YOU SHOULD SEEK ADVICE FROM A COMPETENT TAX ACCOUNTANT OF YOUR CHOOSING FOR APPLICATION OF THIS GENERAL INFORMATION TO YOUR SPECIFIC FEDERAL, STATE, OR LOCAL INCOME TAX RETURN. It should be emphasized that this section has covered only the major tax aspects of your Mary Kay Career and your status as a self-employed person. We have provided this information solely to draw your attention to certain responsibilities and rights which you may have as a taxpayer. Taxes are, however, your personal responsibility and the Company's comments in this area are not intended as tax advice concerning your specific situation.

([illegible] [illegible] of Colgate Palmolive)

A TAXING SITUATION

"I'm proud to be paying taxes in the United States. Problem is, I could be just as proud for about half the money."
Arthur Godfrey

Most of us feel pretty much the way the "ole red head" does about taxes. We're proud to be a part of the railroad, we just wish the fare wasn't so high. At this time of year, we are faced with shouldering our part of the burden while trying to keep from paying someone else's share, too. As an independent contractor, your contribution to the federal coffers may be reduced by taking advantage of certain deductions related to your business. In most states, too, your tax liability may be decreased by advantages offered small businesses. The only way you can really find out exactly what state and federal tax breaks you are entitled to is to sit down and talk with your accountant.

Before you make your appointment, though, prepare yourself to ask, and answer, a lot of questions. Some of the areas you should cover are listed here. There may be others, according to your particular situation. The more you familiarize yourself with federal and state tax forms and instructions booklets, the more possibilities will occur to you. Most of all, keep good records to back up your claims and don't be afraid to ask questions.

One of the more frequent questions asked by self employed persons who work from their homes is "Can I deduct the cost of using my home as my place of business?" Generally, to take this deduction, the IRS expects you to have a room, or a well defined area of a room, that is used regularly and exclusively for your business related activities. If this is the case, you may be able to take a percentage of certain expenses. The percentage allowed will be figured on the percentage of your home which is used for your business. *Some of the expenses you should ask your accountant about are:*

interest paid on your mortgage, improvement loan and insurance
taxes on real estate
repairs and maintenance to the property as a whole and to the office in particular
depreciation
utilities
telephone, both a percentage of local calls made on your home phone for business purposes and all long distance calls for this purpose, also the entire cost of a separate phone used exclusively for your business

For other ideas on home office regulations, refer to Federal Form 2106 and Publication 587, both available from the IRS.

Another question frequently asked about self employment concerns the cost of operating an automobile for business use. In general, costs for such operation are figured on Schedule C, Profit or (Loss) from Business or Profession. Again, your accountant is the one to answer your specific questions about which, if any, of your expenses are deductible. Remember that in any case only the percentage of the expense of operating the car for business purposes is allowable. This is a case where very careful record keeping can make a big difference. You should keep track of

auto taxes and licensing fees
insurance costs
auto club membership fees
maintenance, including oil changes, lubes, tires, cleaning, and so on
parking and toll fees
mileage

Also ask your accountant about the interest you have paid on your car loan and depreciation of the car. New depreciation laws, effective in 1981, may be a boon to you now and through 1983. There is also a liberalized investment credit available for tangible property, including autos, put into use in 1981. Your accountant can explain it to you. Form 3468 must be used to claim this credit and the form is quite complicated. Have your accountant figure out if you should file this form.

In order to conduct your business, you make certain purchases. Keep records, including receipts, of these and ask your accountant about:

merchandise purchased for resale or gifts, awards and prizes
sales kits and samples
office supplies and postage, including promotional materials
books and publications pertaining to your business

In addition to purchasing "things," you may also purchase "services." Some that may qualify for deductions are:

advertising, including newspapers, handbills, radio and yellow page ads (look on your telephone bill for this one)
travel costs such as air and railway fares
hotels and meals while away from home overnight
utilities and telephone costs (Be sure not to deduct on Schedule C if you have already included these in your "office at home" figures.)
contract labor (This applies to monies paid to someone who is not on your payroll but whom you pay to assist you once in a while.) accounting and legal fees

Other expenses you need to ask about are:

interest on business debt
depreciation (and investment credit) on office equipment
cost of entertaining customers
bank service charges
rental fees for safe deposit boxes to contain business records

Also talk to your accountant about additional taxes you may owe as a self employed person. Since you have no employer to deduct federal or state employment taxes from your earnings, you may be obligated to do so yourself. Schedule SE is used for this purpose and your accountant will have to complete your Schedule C first in order to determine your liability, if any. Certain self employed persons must file an estimated tax form every year and make regular payments to the government. Your accountant can help you with this, also.

Finally, one of the biggest tax breaks for self employed persons in the Keough plan. This plan allows you to "shelter" a portion of your earnings and not pay taxes on it until you retire and are in a presumably lower tax bracket. If you haven't discussed this plan with your accountant, now is the time to do so. You'll not only be saving yourself some tax money this year, you'll be building for your future as well.

Doncaster
Rutherfordton, N.C.

By the same token, no area is "guaranteed" exclusive territory of a Saleswoman. Almost all communities have more potential than can be adequately covered by one Saleswoman and additional Saleswomen will be appointed when a District Manager has calculated than an area can support more.

Of course Saleswomen will not be appointed indiscriminately nor without the knowledge of the established Saleswomen, even to comparing potential customer lists if that is necessary.

Experience has proved that when a new Saleswoman is appointed in a community with already established businesses, the sales for everyone invariably improve! Increased exposure is far more valuable than pure exclusiveness.

SALES TAX – Most states, and many municipalities have a Sales and/or Use Tax. Unless you live in one of the states listed below, we urge you to contact your State Sales Tax office for information regarding your responsibilities as an independent business person making sales of merchandise.

In the following states ONLY, Doncaster has an arrangement with the State Revenue Department regarding Sales Tax. On all sales, except when your instructions call for shipment outside of your state, collect and remit to Doncaster the sales tax appropriate. Send this amount to Doncaster with your payment.

Many municipalities have a sales tax . . . if your town or city has such a sales tax and you live in the states listed below, collect and remit to Doncaster the municipality tax as well.

When you are purchasing any Doncaster item at a price less than normal (ex: Personal purchase at 50% of retail) compute the tax on the amount due Doncaster.

The states are: North Carolina, Louisiana, Michigan, Tennessee, South Carolina, Illinois, Georgia, Florida, California and the District of Columbia.

SALESWOMEN WHO RESIDE IN THESE STATES MUST CLEARLY STATE THE DOLLAR AMOUNT OF SALES TAX IN THE PLACE PROVIDED ON THE ORDER FORM.

FEDERAL INCOME TAXES – Since you are an independent business person with business expenses as well as income, Doncaster does not report your income to the Federal government . . . we don't really know what your net income is. You should consult with your own tax consultant on this matter.

Exception: When you earn cash bonuses from Doncaster (as described in the bonus plan) which exceed $600 in a calendar year, it is necessary that we report these cash payments to the Federal government. A copy of the form 1099 is sent to you.

SOCIAL SECURITY – Because you are an independent business person, we feel you should contact either your tax consultant or local Social Security office to learn of your obligations under the Social Security laws.

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DONCASTER SAMPLES – Each season we offer the samples Doncaster provides for sale at discounts published prior to each season. Saleswomen may reserve samples for end of the season delivery (this, too, is defined prior to each season) simply by writing name and account number on the reverse of the hang tag.

It is important that these valuable samples be disposed of, thus the generous discounts offered. But you should exercise care in your handling of sample sales. We urge prudence in making it known that samples may be purchased through you at a discount (you should quote a higher price than Doncaster charges you to make it worthwhile). But . . . only people very close to you and/or carefully selected individual customers should have this knowledge. Your biggest profit opportunities are in conventional sales . . . sample sales are only for special people or situations . . . that includes yourself, of course.

FASHION SHOWS – From time to time, Doncaster will advise you that a set of samples, especially created for conventional fashion shows, is available for your use. If you feel there would be promotional advantages to your business to conduct a Doncaster fashion show for some group or organization, please contact your Sales Service Consultant for information.

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Fortunate Corp.

business performance, is that included in our journals are transactions which have no impact on profit and loss. Our cash flow showed an increase of $1162.34 during the month. When we examine our journals, we find an entry reflecting the personal contribution into the business of $200. Wouldn't you agree that the $1162.34 somewhat overstates business performance during the month? Sure it does!

In this example, the business made less than $1162.34 because included in this figure is a personal contribution of $200.

The second half of the Monthly Activity Schedule lays out the adjustments that must be made to convert cash flow to profit loss. The first change is obvious. The ending cash balance for September includes the ending cash balance from August. To examine September's operation properly, this amount must be pulled out. In the next adjustment, cash added to the business during the month must be subtracted and cash taken from the business must be added back.

The third adjustment is not so obvious. Inventory levels vary from month to month. At any one time, your inventory of products, sales and business aids will consist of the current month's purchases plus inventory carried over from prior months. To accurately reflect your activity in any particular month, a physical inventory must be taken at the end of the month. If the value of the inventory at distributor cost is greater than the prior month, this increase must be added to your cash flow. This addition is necessary because your purchases for the current month reflect inventory that is still on hand and won't be sold until the following month.

Conversely, if the value of the inventory on hand is less than the prior month, this difference must be subtracted from cash flow. This subtraction shows that you not only consumed all of your purchases from the current month, but you dipped into the prior month's as well.

Tax Deductible Business Expenses

The last set of adjustments might possibly be made at the end of the year. But if you want an accurate record of how you are doing, make the adjustments each month.

Depreciation is the business term used to designate the recovery of the cost of an asset with a useful life greater than one year. For example, most aids used to develop business are deductible as a business expense in the year the expense is incurred. Examples would be business stationery, phone charges and newspaper ads. However, for those aids which will tend to benefit the business for a period greater than a year, the government allows only a portion of the cost to be expensed during any year. An example might be a typewriter. The typewriter costs $300 and has a useful life of 3 years (according to the government). Therefore, only 1/3 or $100 would be recoverable as an expense in the current year. The $100 would be recorded as depreciation expense.

The other two adjustments simply refer to expenses you incur in your business for which no check is written or no reimbursement is made. An automotive expense would be such an example.

The government allows a deduction for the business use of your automobile. The deduction is based on a set rate times the number of business miles driven (see section on the tax advantages of your Fortunate business). This figure would appear here. The same applies to your office-in-the-home expenses.

Once you have made all of the adjustments, it is simple to tally everything and come to "the bottom line." This figure represents the profit or loss from your operation during the current month. This figure also will help you track your progress and provide an indication of your level of success in the business. Once you start the system, stick to it. Records will be so much easier for you at the end of the year if you keep to this system.

Tax Advantages Of Your Fortunate Business

Personal taxation is normally an area that few people are willing to discuss. The pervading attitude is generally one of resignation. You know the old saying, "the only real certainties in life are death and taxes."

Being in business for yourself can change that attitude. The federal government is very supportive of the entrepreneural spirit underlying new business. To support this spirit, the government has virtually left untouched areas in the tax law closed to other taxpayers.

Basically, the tax law provides that any ordinary and necessary expense, to the extent that it is directly related to the pursuit of a trade or business, is deductible. To claim the expense, you must be able to verify the nature of the expenditure as being related to your business, and document and support the fact that the expenditure was actually incurred.

To help you maximize the tax advantage of having your own business, a check list of deductible expenditures is provided below. There also are highlights covering the three most common expenses incurred in a Fortunate business: travel and entertainment, office in the home, and automobile expense. Please keep in mind, that this discussion is only to provide a guideline and general overview of the taxation area. If there is any question regarding the deductibility of a business related expenditure please check further with competent tax counsel.

Tax Savings: You Are Eligible

Deductible Expenditures

1) Advertising—flyers, mail pieces, newspaper ads
2) Promotional expenses — contests, awards, plaques, pins
3) Office supplies — pens, pencils, typewriter paper, envelopes
4) Postage
5) Bank charges and check charges
6) Legal and accounting fees
7) Telephone — proportion of basic charges and business related calls
8) Purchase and use of comparable products for quality testing.
9) Dues & subscriptions — local newspaper, nutrition and/or pet periodicals
10) Cost of business meetings — room, refreshments, name tags, banners
11) Proportionate share of home expenses for office in home (see below)
12) Automotive expenses (see below)
13) Travel and entertainment expenses (see below)

This is not an all-inclusive list of deductible business expenses. Remember, the only tests you need to satisfy involve showing 1) that the expenditure was ordinary and necessary to the conduct of your business, 2) that the expenditure was directly related to the conduct of the business and 3) that you can document through receipts that the expenditure was incurred and paid.

Having your own business can result in many tax savings dollars. It is important that you take advantage of these tax savings. It is all a part of being involved in your own Fortunate business.

Office In Home Deduction

(Status of Tax Law at Sept. '80)

As a Fortunate distributor, you are entitled to deduct expenses for maintaining an office in your den or bedroom provided you follow one of these rules:

1) Use a portion of your home **exclusively** and on a regular basis as your principal place of business, or as a place for meeting and dealing with distributors or —
2) Use a portion of your home on a regular basis for the storage of inventory, regardless of whether or not your office is used exclusively for business, but only if this is your only business location.

In both cases, however, the expenses that you can deduct are limited to the net profit of the business before claiming any deduction for your office expenses. Assuming that you operate profitably, you will be able to deduct the following expenses attributable to the portion of your home used as your office:

1) Utilities
2) Interest on your mortgage
3) Insurance
4) Depreciation
5) Repairs
6) Taxes

Remember, however, that to be able to deduct these items, you must A) use a portion of the home **exclusively** as an office, or B) operate only out of your home and use a portion of the home for an office and for storage of inventory. As a Fortunate distributor, you should be able to qualify under the more lenient test in (B) since you will probably store inventory in your home and you will probably only work out of your home.

Let us assume, for example, that Joe Morris is a distributor who uses the den (125 sq. ft.) of his five room house (1000 sq. ft.) as his office and for the storage of the goods he sells. He uses the den approximately 60% of the time for business purposes and the rest of the time the room is used for family purposes. Assume that Mr. Morris' total expenses of maintaing the home are as follows:

Interest	$ 800
Real estate taxes	1200
Utilities	600
Insurance	400
Repairs	550
Depreciation	800
	$4350

Since Mr. Morris does not use his den exclusively for business purposes, two allocations must be made to determine the portion of expenses that can be deducted. The first allocation would be to calculate what portion of the home is used for business. The relative square footage of the den to that of the entire house must be compared to determine the percentage of the home used in the business. In this case, 125 (the size of the den) of the total 1000 square feet in the home is being used and, accordingly, 12.5% (125/1000) of the home expenses would be allocated to the den. In this case, 12.5% of the total expenses of $4,350.00 equals $543.75.

The second allocation required is to adjust for the fact that the den is only used 60% of the time for business. Therefore, 60% of expenses allocable to the den or $326.25 would be deductible by Mr. Morris as business expense. The balance of the interest and real estate taxes, would be deductible in any event as itemized deductions on Schedule A of form 1040. Remember, when computing your home office deduction, that it is limited to the net profit of the business before this deduction.

If Mr. Morris had only netted $250 in the business prior to the home office deduction, of the total otherwise deductible expenses of $326.25, only $250.00 would be deductible. When computing that portion of the $326.25 which is included in the $250 deduction, the Internal Revenue Code requires that the pro rata portion of real estate taxes and interest be deducted first. Thus, the first $150.00 ($800 + 1200 = 2000; 2000 × 60% × 12.5% = $150) of the allowable deduction of $250.00 would be reported as taxes and interest expense. The remaining expenses would be calculated as follows:

Utilities
(600.00 × .125 × .60) = $45.00
Insurance
(400.00 × .125 × .60) = $30.00
Repairs
(550.00 × .125 × .60) = $41.25
Depreciation
(800.00 × .125 × .60) = $60.00
$176.25

Of this total of $176.25, only $100.00 is deductible since the total home office deduction cannot exceed $250.00. In determining which of the above expenses are to be disallowed, depreciation is first. Out-of-pocket ex-

Maximize the Tax Benefits

penses, other than interest and taxes, are deductible in any event. Any interest or taxes disallowed as home office deduction could be deducted on Schedule A as itemized deductions.

In this example, $60.00 of depreciation would be disallowed and $16.25 of repairs, utilities or insurance would be disallowed. Mr. Morris' total deduction would, therefore, equal $250.00 for home office expense.

Remember that to be entitled to an office-in-the-home deduction, you must be able to show that you can satisfy one of the two tests: an area of your home is used exclusively for business or that an area is used for the storage of inventory and an office even though it is also used for personal purposes.

Travel and Entertainment Guidelines

(Status of Tax Law as of Sept. '80)

Travel and entertainment expenses generally comprise travel, meals, lodging, business meetings, entertainment and gifts. As an independent businessperson, it is important that you understand the rules under which the IRS operates, and that you take advantage of the deduction generated from your expenses.

Travel Expense: Imagine hopping in your car and traveling throughout your region recruiting and working with existing distributors! To the extent that your trip is **entirely** for business, your reasonable and necessary travel expenses, including **transportation, meals** and **lodging,** are deductible. If your trip is **primarily** for business, and you extend your stay for non-business reasons, the travel expenses to and from your business destination are deductible. Imagine traveling to Florida for a week from Pennsylvania to build your organization and having the business pay for the trip!

Remember the question of primary purpose is one of fact and is largely determined by the amount of time you spend working on the business compared to your personal activities.

Entertainment Expense: Any activity that is generally considered social or recreational constitutes entertainment. To be deductible, entertainment expenses must be directly related to conducting your business and must be ordinary and necessary to the carrying on of your business. In addition, you must substantiate these expenses by providing recordkeeping that details:

1) The amount of the expenditure
2) The date the entertainment took place
3) The place where you entertained
4) The reason for the entertainment
5) The name(s) of the party(ies) entertained

You must also have receipts which document the actual expenditures.

With regard to being directly related to the business, you must show:

1) That you had a general expectation of deriving income from the party entertained,
2) That you engaged in business during the entertainment period, and
3) That the general mood of the entertainment was related to your business.

With these guidelines, you are well on your way to maximizing the tax benefits of being in business for yourself.

Use Of Your Car In Business

(Status of Tax Law at Sept. '80)

We live in a mobile society. Dependency on automobiles is a very real phenomenon. Just ask any family with kids involved in extracurricular activities. Your involvement in Fortunate undoubtedly has accentuated this dependency. How could you meet and sponsor new distributors, service your existing distributors and retail customers without using your car in the business?

The government realizes this dependency and consequently has provided for the deduction of business-related, transportation expenses. You can take one of two approaches:

Regular: To the extent your car is used in the business, a deduction can be taken for all out-of-pocket expenses incurred for gas, oil, maintenance, insurance and taxes. For example, if you use your car 50% of the time for business (measured by taking business miles divided by total miles driven) and you incurred $1,500 of expenses during the year, $750 could be deducted as a business expense.

Optional: An alternative approach is a standard mileage allowance for business use of your car. The government allows a 20¢/mile allowance for the first 15,000 business miles and 11¢/mile for all business miles in excess of 15,000. This allowance was established to eliminate the need to keep detailed records of expenditures as well as receipts. All you need to support the deduction is a travel log indicating when you traveled; where you traveled; the number of miles and the business purpose behind the trip. At the end of the year, you add up the miles and multiply by the allowance. This figure is your deduction.

To decide which approach is best for you, track them both and make a decision at the end of the year. If you're driving a gas guzzler the regular method might be the most appropriate. If you're getting 40 miles per gallon, go the other way. The government doesn't care which method you choose and you can change your approach from one year to the next. Regardless of the method you use, remember to keep track of tolls and parking fees. These expenses are also deductible as long as they are related to business. So the next time you pull up to the pump, smile! This one's on Fortunate.

THE IRS & YOU

Distributors often write and ask how their Fortunate business affects them from a tax standpoint.

Unless you transfer your distributorship into a corporation or partnership, you will be treated as a sole proprietorship by the IRS (Internal Revenue Service). The income or loss from a sole proprietorship gets included in your personal tax return (form 1040) by completing a Schedule C.

Schedule C is a recap of your income and expenses in your business. This information can be taken from your Fortunate Bookkeeping System (see 152) and transferred to this form. Schedule C, along with many other helpful tax guides can be obtained from your local IRS office. Check the white pages in your phone book under U.S. Government.

In addition to reporting the income or loss from your Fortunate business on your personal tax return, you must notify the government when payments you've made to any of your **personally sponsored distributors** exceeds $600 during the calendar year. This information is reported on Form 1099-Misc. Once again, see your local IRS for additional information.

Briefs Renewal

Our monthly news publication, *The Business Briefs,* is designed as a communication link between home office and the field distributor network. The *Briefs* is our mouthpiece to announce new products, new contests, changes and/or modifications to the Fortunate program, and a place to recognize our leading distributors and Directors. Over the years, the publication has proven to be an effective motivating and recruiting aid.

In addition to informing distributors about new products, product demonstrations, promotional aids, etc. the *Briefs* reports who is active or inactive in our business. This information is in the form of a *Briefs* renewal process which takes place each year. Since it is senseless to continue sending the *Briefs* to someone who isn't seriously involved in the business, our files are cleared each December 31st of distributors who do not renew the *Briefs* for the following year. This is how the process works.

Heritage Corporation of America

Dallas, TX

TAXES

One of the best things about your HCA opportunity is the new ability you have to make money. This is an exciting prospect for everyone. But as an independent Distributor, you are now self-employed and responsible for keeping records of your income and expenses for tax purposes. This is required by law.

Income
Keep receipts for all your retail sales and any product refunds. It really doesn't take long to write up a receipt. And if you don't keep an accurate record of retail and wholesale amounts for the year, you will have the very unpleasant task, at the end of the year, of going back and trying to figure it out all at once. If you have a separate business checking account, you should also keep a record of all money deposited that comes from sources other than HCA sales or Wholesale Volume Bonuses (WVB).

Travel
Keep a record of your mileage. You should also show the purpose of the trip. Additionally, keep a record of actual expenses. In many cases, expense plus depreciation will come out better than the standard deduction.

Entertainment
Keep receipts. Enter person entertained and purpose.

Telephone
Deductions allowed on a portion of your monthly service charge plus long distance.

Cash business expenditures
Keep receipts on all postage, printing, office supplies, etc. List purpose for purchase. When it comes time to file your annual tax statement, you will find the task much more pleasant if you have kept your records and receipts as neat and organized as possible. You can save yourself time and money by setting up a simple ledger, listing each week's expenses, income, etc. By keeping your receipts in order and up-to-date, your information will be easy to translate into the proper categories for tax deductions.

Tax Savings
Office at Home — Deduction allowed only if entire room is used exclusively and frequently for business purposes.

Investment credit —
Available if you have a child at home who is a full time student or under 19. You can pay them to work for you and still claim them on your taxes provided they earn less than $2,950.

Spouse — You can pay your spouse and his or her wages are not subject to Social Security. It is a business deduction, but it must be paid on a regular basis and by check, and it must be a reasonable amount of compensation.

FIRST THINGS FIRST

As an independent business person, you'll want to give some thought to the business side of your career. You make your own plans and keep your own records. You conduct your own affairs, organize your own time and come and go as you please. Here are a few suggestions you may want to consider.

THE BASICS

Your Sample Kit The kit contains everything you'll need to start your business. Over $150 in color coordinated INGRID products and all the literature you will need for your first few shows. Certainly you'll need such things as postage stamps, and perhaps the rubber name stamp described on page 2. You'll want to be aware of your supplies and reorder in enough time so that you don't run out of them.

You might want to start thinking about the things you'll need for your first month in business. Especially such things as Customer Orders, Order Summaries, Invitations and Catalogs. You'll also want more linen swatches and color chips and items to use as gifts or prizes at your shows. All of these items are on the INGRID AT HOME Supply List and can be ordered on a Sample and Supply Order form. Allow ten to twelve days for delivery of supplies.

You'll want to start adding samples to your kit and they're available at a generous 50% discount. These samples as well as your Sample Kit and all supplies are tax deductable.

Record Keeping This is easy and a composition book will be all you need. You'll want to record your ordinary business expenses such as stamps, supplies, telephone, etc., and also auto expenses. Open to the first two facing pages and title one side "Expenses" and the other side "Auto Log".

EXPENSES Date Item Amount

AUTO LOG Date Destination Reason Mileage

Taxes No deductions will be taken from your earnings. It's your responsibility to pay your state and federal income tax. That's why record keeping is important — you're entitled to many legitimate deductions. For instance, the cost of your Sample Kit, supplies and your share of the Hostess Award are deductable. Annually, you'll receive a 1099 form from INGRID indicating your total earnings.

If you are not already using an accountant, you might want to consider one. The fee is deductable and the savings on your taxes could be quite worthwhile.

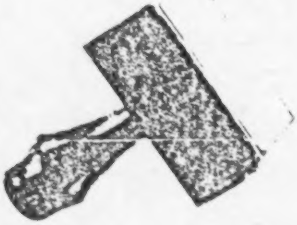
INGRID
AT HOME

A Separate Checking Account It's just good business! Deposit your earnings and keep track of your expenses. It should be in your name, not INGRID AT HOME.

Sales Tax You are responsible for remitting the proper amount, based on the correct tax rate, to the Company. This is collected from the customer and shown on the Customer Order. INGRID AT HOME will forward the tax to the proper State taxing authority. This eliminates your need for a sales tax number and the related paper work. [illegible]

Your Datebook Use a datebook to record everything you have to do — both business and personal. Use it for recording your Shows, meetings, visits to the doctor or dentist, PTA meetings, everything that is part of your schedule. In this way you will always be where you should be when you should be.

A Rubber Stamp Here's a real timesaver. Every piece of literature meant to be left with someone has a place for your name, Rep number, address and telephone number. All Customer Orders should contain the same information. Using a name stamp is a lot faster and much more businesslike.



Susan Archer 000/000
201 Main Street
Anytown, U.S.A. 98765
(123) 456-7890

Know Your Line Get to know the products in your Sample Kit. How they work together, various uses for the different items, colors available and prices. Go through the catalog and work with the Product Guide to know the basics about each item in the line. You do not have to memorize everything, but you should be familiar with them.

The more you know about the line, the more success you will have in presenting it. We all like to do business with people that care enough about what they are doing to become knowledgeable about the products in their line. We have a lot more confidence and feel much more comfortable doing business with them.

It's a good idea to set up a master catalog. In it, mark the price of each item and also anything special you want to make note of. Circle each item for which you have a sample and use this as a guide in conducting your Shows.

You may want to take the Show Sequence and the Product Sequence that is contained in this guide (pages 49-51) and tape it into your master catalog. Mark the cover of the catalog with the word "Master". HAVING THE PRODUCT GUIDE WITH YOU (PAGES [illegible]) WOULD ALSO BE HELPFUL.

INGRID
AT HOME

Oriflame

BOOKKEEPING

Income Tax Benefits

As an independent sales person, you are considered to be self-employed. As such, there are several income tax deductions available to you and your husband as a result of your business activities. Remember to keep accurate records and the expense receipts to justify all deductions!

Keep all expense receipts and list on each of them the item purchased. Set up a set of books and keep continuously track of your sales and expenses. If you keep your bookkeeping in order from the start, it will be very easy for you.

It is a good idea to have an accountant prepare your annual tax return. He will be able to guide and inform you of all deductions that are available to self-employed persons.

WHO'S WHO IN DIRECT SELLING

DIRECT SELLING ASSOCIATION • 1730 M ST., N.W., WASHINGTON, DC 20036 • 202/293-5760 • 202/466-5760

ACTIVE MEMBER COMPANIES AS OF MAY 7, 1982

ABI, Inc.
(2)
339 East 16 Street
Holland, MI 49423
Jack G. Stewart
(616) 392-7141
Buyers service

Alfa Metalcraft Corporation of America
(1)
7970 Bayberry Road
Suite 10
Jacksonville, FL 32216
Sue K. Clark
(904) 731-8200
Cookware

Aloe Magic, Div. of Exalo Tech. Corp.
(1)
2828 East 55 Place
P.O. Box 20423
Indianapolis, IN 46220
Sandra Maurer Budnick
(317) 253-3638
Cosmetics

American Dream International Inc.
(2)
360 South Hope Avenue
Suite 100
Santa Barbara, CA 93105
Donald L. Thompson
(805) 569-1221
Cosmetics

Amway Corporation
(2)
7575 East Fulton Road
Ada, MI 49355
William J. Halliday, Jr.
(616) 676-6000
Household products

Arbonne International, Inc.
(2)
530 West 9460 South
Sandy, UT 84070
Gordon Pearson
(801) 566-5124
Cosmetics

Aubrey McDonald Creations, Inc.
(1)
565 Wolf Ledges Parkway
Akron, OH 44311
Duane L. Barnes
(216) 376-4122
Fashion jewelry

Aura, Ltd.
(2)
2454 Dempster Street
Des Plaines, IL 60016
Manfred Esser
(312) 299-6640
Wine

Avacare, Inc.
(1)
9200 Carpenter Freeway
Dallas, TX 75247
Clinton H. Howard
(214) 638-7686
Cosmetics

Avon Products, Inc.
(2)
Nine West 57 Street
New York, NY 10019
James E. Preston
(212) 546-6015
Cosmetics

BeautiControl, Inc.
(1)
2101 Midway Road
P.O. Box 345189
Dallas, TX 75234
Richard W. Heath
(214) 458-0601
Cosmetics

Bel Kraft International, Ltd.
(2)
32431 Schoolcraft Road
Livonia, MI 48150
Raymond D. Bechard
(313) 522-8556
Cookware

Better Living Products, Inc.
(1)
495A Busse Road
Elk Grove Village, IL 60007
Judy Skoney
(312) 956-0900
Household products

Bon Del Inc.
(2)
3716 East Main Street
Mesa, AZ 85205
Ray E. Ward
(602) 955-0980
Houseware specialties

Cameo Coutures, Inc.
(2)
9109 Carpenter Freeway
P.O. Box 47390
Dallas, TX 75247
J. Stanley Fredrick
(214) 631-4860
Clothing

Care Free International Inc.
(1)
1725 Hurd Drive
Irving, TX 75062
L. Scott McKnight
(214) 258-1240
Food supplements

Castlebleu, Inc.
(1)
680 Spring Street
North Dighton, MA 02764
David Stormer
(617) 824-1444
Decorative accessories

Cattani of California
(1)
11842 Hamden Place
Santa Fe Springs, CA 90670
Bettie Kanelos
(213) 949-8466
Clothing

Ceres Cosmetics, Inc.
(1)
201 College Avenue
Salem, VA 24153
Leon Mitchell
(703) 387-2275
Cosmetics

Chambre' Cosmetic Corporation
(1)
P.O. Box 7777
Chatsworth, CA 91311
Eric V. Berry
(213) 998-3322
Cosmetics

Community World, Inc.
(1) (2)
5351 Naiman Parkway
Solon, OH 44139
Joseph P. Lemire
(216) 248-7370
Household products

Concept Now Cosmetics by Rita Gross
(1)
14000 Anson Street
Santa Fe Springs, CA 90670
Eva McClintock
(213) 921-0534
Cosmetics

Con-Stan Industries, Inc.
(1) (2)
19501 Walnut Drive
City of Industry, CA 91748
Mulford J. Nobbs
(714) 598-1831
Household products

Coppersmith Company
(1)
7500 Bluewater, N.W.
Albuquerque, NM 87104
Maynard Cowan
(505) 831-4519
Decorative accessories

The Creative Circle
(1)
15777 South Broadway
Gardena, CA 90248
George H. Karlin
(213) 327-1931
Craft products

Creative Expressions
(1)
East Meadow Avenue
Robesonia, PA 19551
Peter DeBlasi
(215) 693-3191
Craft products

Daisy Fashion Jewelry
(1)
1334 Lincoln Avenue
San Jose, CA 95125
Pam Grein
(408) 289-8313
Fashion jewelry

Dermique Cosmetics Corporation
(1)
16116 Cohasset Street
Van Nuys, CA 91406
Hal L. Avery
(213) 902-1075
Cosmetics

Destiny Products, Inc.
(2)
3880 State Street
Santa Barbara, CA 93105
Robert L. Skelton
(805) 687-6221
Cosmetics

Diamite Corporation
(1)
131-D Albright Way
Los Gatos, CA 95030
Ralph M. Flynn, Jr.
(408) 866-7100
Jewelry

Discovery Toys, Inc.
(1)
1845 Park Road
Benicia, CA 94510
Lane Nemeth
(707) 745-6464
Toys

Doncaster
(1)
Box 1159
Rutherfordton, NC 28139
Charles L. Benedict
(704) 287-4205
Clothing

Dudley Products Company
(2)
50 East 26 Street
Chicago, IL 60616
Joe Louis Dudley
(312) 326-5800
Cosmetics

Duskin-California Inc.
(2)
108E Star of India Lane
Carson, CA 90746
K. Imahara
(213) 770-8706
Household products

Elegant Cosmetics, Inc.
(1)
202 West McNeese Street
Lake Charles, LA 70605
David Bertrand
(318) 474-0505
Nutritional products

Encyclopaedia Britannica, Inc.
(2)
425 North Michigan Avenue
Chicago, IL 60611
Charles E. Swanson
(312) 321-7111
Educational publications

Enhance Corporation
(2)
125 Ryan Court
Suite 202
San Ramon, CA 94583
Robert J. Wooten
(415) 820-9300
Food supplements

Fashion Two Twenty, Inc.
(1)
1263 South Chillicothe Road
Aurora, OH 44202
Keith George
(216) 562-5111
Cosmetics

Fortunate Corporation
(2)
P.O. Box 5064
Charlottesville, VA 22905
Rick Goings
(804) 977-5720
Animal preparations

The Fuller Brush Company
(2)
2800 Rock Creek Parkway
Suite 400
Kansas City, MO 64117
Len D. Dunlap
(816) 474-1754
Household products

Future Craft Enterprises, Inc.
(2)
1283 Broad Street
Bloomfield, NJ 07003
Vincent E. Dima
(201) 575-5475
Cookware

Grace Unlimited, Incorporated
(1)
14430 East Valley Boulevard
City of Industry, CA 91746
Grace Batts
(213) 961-9481
Cosmetics

Grolier Incorporated
(2)
Sherman Turnpike
Danbury, CT 06816
Richard Clark
(203) 797-3500
Educational publications

The Hanover Shoe, Inc.
(2)
111 North Forney Avenue
Hanover, PA 17331
Thomas G. Sexton
(717) 632-7575
Shoes

Health-Glo, Inc.
(1) (2)
6689 Peachtree Industrial Boulevard
Suite P
Norcross, GA 30092
James P. Roberts
(404) 447-5292
Cosmetics

Heritage Corporation of America
(1)
P.O. Box 401209
Dallas, TX 75240
C. Craig Keeland
(214) 385-1710
Food supplements

Highlights for Children, Inc.
(2)
2300 West Fifth Avenue
Columbus, OH 43216
Richard H. Bell
(614) 486-0631
Educational publications

Home Accents Unlimited, Inc.
(1)
P.O. Box 1589
Lima, OH 45802
Charles Crockett, III
(419) 228-9911
Craft products

Home Decorating Associates, Inc.
(1)
P.O. Box 35888
Tulsa, OK 74135
William E. Kenney
(918) 252-1661
Decorative accessories

Home Interiors & Gifts, Inc.
(1)
4550 Spring Valley Road
Dallas, TX 75234
Mary C. Crowley
(214) 386-1000
Decorative accessories

House of Lloyd, Inc.
(1)
11901 Grandview Road
Grandview, MO 64030
Harry J. Lloyd
(816) 763-7272
Toys

Hy Cite Corporation
(1)
340 Coyier Lane
Madison, WI 53713
Peter O. Johnson
(608) 271-6363
Cookware

Ingrid at Home
(1)
3601 North Skokie Highway
North Chicago, IL 60064
Karen Mitcham
(312) 578-7512
Housewares

Jackie Brown, Inc.
(1)
220 North Story Road
Suite 108
Irving, TX 75061
Jackie Brown
(214) 259-3717
Cosmetics

Jafra Cosmetics, Inc.
(1)
P.O. Box 5026
Westlake Village, CA 91359
Thomas C. Grant
(213) 991-4360
Cosmetics

The Kirby Company
(Scott Fetzer)
(2)
14600 Detroit Avenue
Cleveland, OH 44107
Ralph Schey
(216) 228-6200
Vacuum cleaners

Lady Finelle Cosmetics
(1)
1376 River Street
P.O. Box 227
Haverhill, MA 01831
Dorothy L. Feigenbaum
(617) 372-8591
Cosmetics

Lady Love Cosmetics, Inc.
(1)
4503 Best Line Road
P.O. Box 1043
Addison, TX 75001
E. Don Lovelace
(214) 233-7010
Cosmetics

Laura Lynn Cosmetics, Inc.
(1)
5456 McConnell Avenue
Suite 189
Los Angeles, CA 90066
Betty Jo Toccoli
(213) 306-4540
Cosmetics

Life Products Corporation
(2)
2340 South El Camino Real
Suite 18
San Clemente, CA 92672
Donald R. Marabella
(714) 492-0273
Food supplements

Lucky Heart Cosmetics, Inc.
(2)
390 Mulberry Street
Memphis, TN 38101
Paul Shapiro
(901) 526-7658
Cosmetics

Mary Kay Cosmetics, Inc.
(1)
8787 Stemmons Freeway
Dallas, TX 75247
Monty C. Barber
(214) 630-8787
Cosmetics

Mason Shoe Manufacturing Company
(2)
21 East Grand Avenue
Chippewa Falls, WI 54729
Bernard Sokup
(715) 723-1871
Shoes

McConnon & Company
(2)
McConnon Drive
Winona, MN 55987
Vilas W. Rogers
(507) 452-2910
Household products

McHoven Products, Inc.
(1) (2)
7333 East Monterey Way
Suite 13
Scottsdale, AZ 85251
Donald F. McIntosh
(602) 941-1075
Cosmetics

Miracle Maid
(1)
(Rena-Ware Distributors, Inc.)
P.O. Box 913
Bellevue, WA 98009
Philip Lindquist
(206) 453-2300
Cookware

Moorman Manufacturing Company
(2)
1000 North 30 Street
Quincy, IL 62301
Ross Warden
(217) 222-7100
Animal preparations

Natural Impressions Corporation
(1)
182 Liberty Street
Painesville, OH 44077
George R. Eierman
(216) 357-8950
Jewelry

NaturaLife International
(1)
P.O. Box 2020
Provo, UT 84601
Dean Black
(801) 377-3093
Food products

Neo-Life Company of America
(1) (2)
P.O. Box 5015
Hayward, CA 94540
Donald Pickett
(415) 786-3401
Household products

Olde Worlde, Inc.
(1)
401 Fraley Road
High Point, NC 27263
Kenneth W. Mackovic
(919) 889-1661
Household products

OMA Products Corporation
(2)
2546 Tenth Street
Berkeley, CA 94710
Keith Van Hoff
(415) 644-2114
Food supplements

Oriflame Corporation
(1)
76 Treble Cove Road
North Billerica, MA 01862
Peter Nawrocki
(617) 663-2700
Cosmetics

Partylite Gifts
(1)
Building 16
Cordage Park
Plymouth, MA 02360
Ruben G. Deveau
(617) 746-6104
Decorative accessories

Perfume Originals, Inc.
(1)
45 West 34 Street
New York, NY 10001
Joseph J. Freedman
(212) 695-9494
Fragrances

Philippine Imports, Inc.
(1)
Eight 'B' Street
Hyde Park, MA 02136
Irene Zuffante
(617) 364-3880
Decorative accessories

PlantMinder, Inc.
(1) (2)
22582 Shannon Circle
Lake Forest, CA 92630
Angela Colella
(714) 951-1123
Plant self-watering containers

Pola U.S.A. Inc.
(1) (2)
250 East Victoria Avenue
Carson, CA 90746
Isao Sato
(213) 770-6000
Cosmetics

Princess House, Inc.
(1)
455 Somerset Avenue
North Dighton, MA 02764
Robert J. Haig
(617) 823-0713
Decorative accessories

Queen's-Way to Fashion, Inc.
(1)
2500 Crawford Avenue
Evanston, IL 60201
James G. Davis
(312) 492-1400
Clothing

The W.T. Rawleigh Company
(1) (2)
223 East Main Street
Freeport, IL 61032
Merrill G. Bowers
(815) 232-4161
Household products

Regal Ware, Inc.
(2)
Kewaskum, WI 53040
Gilbert D. Flocker
(414) 626-2121
Cookware

Rena-Ware Distributors, Inc.
(2)
P.O. Box 913
Bellevue, WA 98009
Philip Lindquist
(206) 453-2300
Cookware

Rose Joyce Cosmetics
(1)
13037 Dorothy Drive
Philadelphia, PA 19116
Rose Joyce Zacharko
(215) 677-8770
Cosmetics

Saladmaster, Inc.
(2)
131 Howell Street
Dallas, TX 75207
Gary J. McDonald
(214) 742-2222
Cookware

SASCO
(1)
P.O. Box 340300
Dallas, TX 75234
Jack W. Shuford
(214) 484-3950
Cosmetics

Shaklee Corporation
(1) (2)
Shaklee Terraces
444 Market Street
San Francisco, CA 94111
Bruce Hasenkamp
(415) 954-2090
Food supplements

Society Corporation
(1)
1609 Kilgore Avenue
Muncie, IN 47304
Foster D. Adams
(317) 289-3318
Cookware

The Southwestern Company
(2)
P.O. Box 820
Nashville, TN 37202
Jerry Heffel
(615) 790-4000
Educational publications

Stanley Home Products, Inc.
(1)
333 Western Avenue
Westfield, MA 01085
H. L. Tower
(413) 562-3631
Household products

The Stuart McGuire Company, Inc.
(2)
115 Brand Road
Salem, VA 24156
E. Cabell Brand
(703) 389-8121
Shoes

Sybil's
(1)
9034 Natural Bridge Road
St. Louis, MO 63121
Fraeda Kopman
(314) 993-0695
Jewelry and fragrances

Tiara Exclusives
(1)
Dunkirk, IN 47336
James E. Hooffstetter
(317) 768-6789
Decorative accessories

Time-Life Books, Inc.
(2)
777 Duke Street
Alexandria, VA 22314
Carol Flaumenhaft
(703) 960-5110
Educational publications

Tomorrow's Treasures, Inc.
(2)
111 North Glassboro Road
Woodbury Heights, NJ 08097
George W. Braun
(609) 468-5656
Photo albums

Total Success, Inc.
(1) (2)
7975 North Hayden Road
Suite A-201
Scottsdale, AZ 85258
Mary Etta Moore
(602) 998-3860
Cosmetics

Tri-Chem, Inc.
(1)
One Cape May Street
Harrison, NJ 07029
Saul Skoler
(201) 482-5500
Craft products

U.S. Safety & Engineering Corporation
(2)
2365 El Camino Avenue
Sacramento, CA 95821
H. Wayne Boyd
(916) 482-8888
Security systems

UndercoverWear, Inc.
(1)
66 Concord Street
North Reading, MA 01864
Walter J. James
(617) 935-0130
Clothing

Unique Decor
(1)
P.O. Box 491
Mansfield, MA 02048
Eliot Kraft
(617) 543-2470
Decorative accessories

United Consumers Club, Inc.
(2)
8450 South Broadway
Merrillville, IN 46410
Fred A. Wittlinger
(219) 736-1100
Buyers service

United Laboratories of America, Inc.
(2)
1526 Fort Worth Avenue
P.O. Box 4499, Station A
Dallas, TX 75208
Bill Sparks
(214) 741-4461
Photo albums

Visions Now
(1)
(Division of Sykes Brothers, Inc.)
4200 Mitchell Street
Philadelphia, PA 19128
David Vanderslice
(215) 482-4433
Crafts

Vita Craft Corporation
(2)
11100 West 58 Street
Shawnee, KS 66203
Dale Ashley
(913) 631-6265
Cookware

Vorwerk USA Inc.
(1) (2)
700 Northlake Boulevard
Altemonte Springs, FL 32701
Eric Levine
(305) 339-8321
Food processors

Watkins Incorporated
(2)
150 Liberty Street
Winona, MN 55987
Richard Wantock
(507) 457-3300
Household products

The West Bend Company
(2)
400 Washington Street
West Bend, WI 53095
Earl P. Mantz
(414) 334-2311
Cookware

World Book, Inc.
(2)
510 Merchandise Mart Plaza
Chicago, IL 60654
Elaine E. Rose
(312) 245-3456
Educational publications

Worldwide Cosmetics Inc.
(1)
676 St. Clair Street
Room 1920
Chicago, IL 60611
Timothy J.Y. Ree
(312) 266-9854
Cosmetics

Zondervan Book of Life
(2)
P.O. Box 6130
Grand Rapids, MI 49506
Rex Jones
(616) 459-7295
Educational publications

According to the bylaws of the Direct Selling Association, those eligible for active membership are persons or firms manufacturing or dealing in merchandise intended ultimately to reach the consumer through an in-person contact, as distinguished from sales contacts made by mail or in stores of the seller. An active member must also have a business location in the United States.

DISTRIBUTION METHOD CODE

Following each company name is a numerical code which indicates the primary method of direct selling used by the company. (1) represents party-plan sales, and (2) represents person-to-person sales.

EXECUTIVE CONTACT:

The person designated under each company listing is the EC (executive contact). This is the individual in the member company designated as the liaison to DSA.

PARENT COMPANIES:

Parent companies are listed in parentheses after the name of the member company. Contact the Member company itself for additional information.

KEY SUPPLIERS TO DIRECT SELLING

DIRECT SELLING ASSOCIATION • 1730 M ST., N.W., WASHINGTON, DC 20036 • 202/293-5760 • 202/466-5760

ASSOCIATE MEMBER COMPANIES AS OF February 1, 1981

A & B Bag Company
Balch Springs, TX
Business & desk accessories/luggage

Advertising & Marketing Associates
Waco, TX
Printing

Alden Press Inc.
Elk Grove Village, IL
Printing

Dick Appelbaum Company
Maitland, FL
Premium/incentive representatives

Arcata Corporation
Stamford, CT
Publishing

Automotive Rentals, Inc.
Maple Shade, NJ
Auto leasing

Badge Man International, Ltd.
Santa Ana, CA
Printing

Bank of Virginia - Bank Card Division
Richmond, VA
Financial services

Martin H. Bauman Associates
New York, NY
Consultants/marketing agencies

The Jas. A. Beakey Company, Inc.
Minneapolis, MN
Business & desk accessories/luggage

Beneficial Management Corporation
Morristown, NJ
Financial services

Ronald A. Bernstein & Associates, Inc.
Chicago, IL
Consultants/marketing agencies

Bissell Inc.
Grand Rapids, MI
Electric floor care

Jonathan Bradley Pens, Inc.
Long Island City, NY
Writing instruments

Brand Edmonds Welch
Salem, VA
Consultants/marketing agencies

Brown Printing Company, Inc.
Waseca, MN
Printing

Burwood Products Company
Chicago, IL
Home-related products

Al Carlisle & Associates
New York, NY
Premium/incentive representatives

Cooper Marketing Associates
Bridgeport, CT
Decorative accessories

Creative Awards by Lane
Elk Grove, IL
Premium/incentive representatives

Creative Marketing Concepts, Inc.
Cleveland, OH
Home-related products

Custom Conventions
New Orleans, LA
Travel

Custom Products Corporation
Tempe, AZ
Business & desk accessories/luggage

Debt Collectors, Inc.
Houston, TX
Financial services

Direct Mass Marketing, Inc.
New Rochelle, NY
Group insurance programs

R.R. Donnelly & Sons Company
Chicago, IL
Printing

DuBarry-Fifth Avenue, Inc.
Brooklyn, NY
Jewelry

Duveen Soap Corporation
Brooklyn, NY
Cleaning supplies/equipment & soap

George E. Dych
Dallas, TX
Training/motivational materials

Ellis & Guy Advertising, Inc.
Omaha, NB
Consultants/marketing agencies

Encyclopaedia Britannica, Inc.
Chicago, IL
Books

The Eureka Company
Rosemont, IL
Cleaning supplies/equipment & soap

Fabrik fur Haushaltgerate
WEST GERMANY
Home-related products

Fairmont Hotel Company
Washington, DC
Hotels

J.G. Ferguson Publishing Company
Chicago, IL
Books

G.B. Frank Incorporated
Chicago, IL
Consultants/marketing agencies

Gibson Amerada Ltd.
Naples, FL
Consultants/marketing agencies

The Graphic Corporation
Des Moines, IA
Publishing/graphics

B.B. Greenberg Co.
Providence, RI
Jewelry

GWV Travel Inc.
Newton Centre, MA
Travel

The Hanover Shoe, Inc.
Hanover, PA
Shoes

Hazel, Inc.
Washington, MO
Business & desk accessories/luggage

The Hewitt Soap Company
Dayton, OH
Cleaning supplies/equipment & soap

Hillestad Corporation
San Jose, CA
Manufacturing chemist

Richard A. Holstein Company, Inc.
New York, NY
Home-related products

Hunter International
Coventry, RI
Jewelry

Hyatt Hotels Corporation
Washington, DC
Hotels

ICS International Travel, Inc.
San Francisco, CA
Travel

Ikelheimer-Ernst, Inc.
New York, NY
Business & desk accessories/luggage

Imperial Pearl Company
Providence, RI
Jewelry

Income Opportunities Magazine
Chicago, IL
Magazines

Indiana Glass Company
Dunkirk, IN
Home-related products

International Flavors & Fragrances, Inc.
New York, NY
Fragrances/essences

Jewels by Felice Inc.
Johnston, RI
Jewelry

Josten's
Minneapolis, MN
Awards/mementos

Klitzner Industries, Inc.
Providence, RI
Jewelry

Knox Associates, Inc.
Fort Myers, FL
Consultants/marketing agencies

Kranzten Studio, Inc.
Chicago, IL
Audiovisuals/graphics

Kranzten-Gould Studios, Inc.
New York, NY
Audiovisuals/graphics

W.A. Krueger Company
Brookfield, WI
Printing

Libbey Glass, Owens-Illinois, Inc.
Toledo, OH
Home-related products

Little Pictures Inc.
Glendale, CA
Home-related products

Loews Anatole Dallas
Dallas, TX
Hotels

Mademoiselle Promotions, Ltd.
New York, NY
Furs

Malco Products, Inc.
Barberton, OH
Cleaning supplies/equipment & soap

Marlborough Jewels, Inc.
Brooklyn, NY
Jewelry

Marriott Corporation
Arlington, VA
Hotels

The MCB Company
Northampton, MA
Premium/incentive representatives

MFI Art Company
San Francisco, CA
Decorative accessories

Mechanical Mirror Works Inc.
New York, NY
Decorative accessories

Mirro Aluminum Company
Manitowoc, WI
Home-related products

Money Making Opportunities Magazine
Studio City, CA
Magazines

Multinational Prints
Los Angeles, CA
Home-related products

Munsey Products, Inc.
Little Rock, AR
Home-related products

National Business Systems Inc.
New York, NY
Plastic card embossers/imprinters

National Computer Systems
Minneapolis, MN
Optical mark scanners

North American Philips Lighting Corporation
Hightstown, NJ
Lighting equipment

Notifier Company
Torrance, CA
Security systems

Oliver and Rozner Associates, Inc.
New York, NY
Consultants/marketing agencies

Oneida, Ltd.
Oneida, NY
Home-related products

Piscitelli Inc.
Providence, RI
Jewelry

Potential Profits Group, Inc.
Branford, CT
Premium/incentive representatives

Professional's Alliance, Inc.
Irving, TX
Consultants/marketing agencies

The Profit Adviser
Maitland, FL
Consultants/marketing agencies

C. Ray Randall Manufacturing Company
North Attleboro, MA
Jewelry

Regal Ware, Inc.
Kewaskum, WI
Home-related products

Reha Glass
Muncie, IN
Home-related products

Relief Printing Corporation
Los Angeles, CA
Printing

Response Graphics
Park Ridge, IL
Printing

Riekes Crisa Corporation
Omaha, NB
Home-related products

Risdon Enterprises, Inc.
Columbia, SC
Home-related products

Roure Bertrand Dupont, Inc.
Teaneck, NJ
Fragrances/essences

Royal Publishers
Nashville, TN
Printing

Salesman's Opportunity Magazine
Chicago, IL
Magazines

Seagull Laboratories Inc.
Salt Lake City, UT
Home-related products

Sexton Metalcraft, Inc.
Raytown, MO
Home-related products

Simon & Schuster/
Pocket Books
New York, NY
Printing

Smith Sales
Corporation
Pleasanton, CA
Jewelry

Spare Time Magazine
Milwaukee, WI
Magazines

Specialty Salesman and
Busines Opportunities
Magazine, Inc.
Chicago, IL
Magazines

Stevens, Inc./Advertising
Grand Rapids, MI
Consultants/marketing agencies

Wm. Stroh, Inc.
West New York, NJ
Consultants/marketing agencies

Success Unlimited
Magazine
Chicago, IL
Magazines

Sunbeam Appliance
Company
Oak Brook, IL
Home-related
products

Syroco
Syracuse, NY
Home-related
products

Texar Corporation
Columbia, SC
Consultants/marketing agencies

Time-Life Books
Alexandria, VA
Books

Travellers Premium
Company, Inc.
New York, NY
Premium/incentive
representatives

Uncas Manufacturing
Company
Providence. RI
Jewelry

Universal Scheduling
Company
Bala Cynwyd, PA
Consultants/marketing agencies

Von Nash Associates,
Inc.
Austin, TX
Consultants/marketing agencies

Warsaw Photographic
Associates Inc.
New York, NY
Audiovisuals/graphics

Washburn Associates,
Inc.
Chicago, IL
Consultants/marketing
agencies

Wear-Ever Aluminum,
Inc.
Chillicothe, OH
Home-related
products

The West Bend
Company
West Bend, WI
Home-related
products

Western International
Hotels
Washington, DC
Hotels

Paul Yamamoto/Daito
Kogyo Co., Ltd.
Tokyo, JAPAN
Vibron electrical
massagers

The Zig Ziglar Corp.
Dallas, TX
Training/motivational
materials

Mr. OFFEN. Basically, to summarize some of the relevant factors, these are people who are in the business to earn a small amount of money, generally speaking, to supplement a family income.

They are in it for a specific objective, to buy Christmas present money, or to buy clothes when the kids go back to school, and they only work a portion of the year. Only 89 percent work part time. So the basic nature of the business is in conflict with the allegation that——

Chairman STARK. The person they suspect, the mythical person that I want to describe is a highly paid professional who is married and his or her spouse has no job. They decide that by buying a cosmetic sales kit for $25 or a home products kit for $100, that is all they have to do to suddenly have a business.

Most of us who might want to establish a business have to rent a store or take some training, but here is instant business, for a very modest amount of money. As the return showed, they never really do sell. Those returns were people who have done the same kind of thing 2 or 3 years in a row.

It is suddenly a way to save $2,000 or $3,000 a year in taxes, to write off the car, write off the convention trip and without, in my opinion, the faintest intent to get out and really hustle and sell to earn a good living, as so many of your members do.

That is exactly the person that I think both of you would agree with me, am I not correct, that we ought to discourage from getting into the business to use it as a tax deduction.

Mr. OFFEN. Yes, we do agree with you on that.

Chairman STARK. I think you and I, the chairman of Amway, and the Commissioner of Internal Revenue would agree right down the line, that if we could find a rule that would discourage them and encourage everybody else, we would all endorse it.

Believe me, that is I think what is behind this committee and our staff's intent. That is going to be tricky. I think we could all agree on where the person who is violating the spirit of the law, and perhaps the letter, I think we can all—you and I—identify that in a broader theory.

How you write a rule that sorts the wheat from the chaff in this case I think is pretty tricky. I would appreciate the help you and your staff could come up with because I think you have worked with this committee long enough to know that we would like to keep things as simple as possible. That is usually the best law and the best kind of rule, and gets the best compliance.

Mr. OFFEN. Even in the worst case scenario I know you would be talking about a miniscule number of people. So it would be crucial that any legislative proposals that come forward would take that into consideration and not put roadblocks or barriers into the income opportunities our industry does for the American people, especially in this time of high unemployment.

Chairman STARK. That you, gentlemen, very much for your cooperation, and thank you for what I anticipate will be your cooperation as we have speedy hearings to get through this whole question of independent contractors in the months ahead.

Mr. OFFEN. Thank you, Mr. Chairman. I would also like to express our appreciation to your staff for the contacts they made and communications they had with us to try to help us to get ready.

Chairman STARK. Thank you very much. They are a good staff, and they work hard. The subcommittee is adjourned subject to the call of the Chair.

[Whereupon, at 5 p.m. the subcommittee adjourned.]

[The following was submitted for the record:]

SHAKLEE

J. Gary Shansby

President
Chief Executive Officer

May 21, 1982

The Honorable Pete Stark
Chairman of the Subcommittee
on Select Revenue Measures
1136 Longworth House Office Bldg.
Washington, D.C. 20515

Dear Mr. Stark:

Attached is my statement for inclusion in the record of your hearing on April 19, 1982 regarding the "deductibility of certain expenses incurred by self-employed individuals."

We do not condone excessive tax deductions and we believe that the vast majority of Shaklee Distributors are only interested in claiming tax deductions which are permitted by law.

We support your efforts to resolve this problem and will continue to provide our assistance in this regard.

Sincerely,

J Gary Shansby

J. Gary Shansby

JGS:mtk

Shaklee Corporation 444 Market Street San Francisco, California 94111 Phone (415) 954-2700

STATEMENT OF J. GARY SHANSBY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, SHAKLEE CORP.

Mr. Chairman and Members of the Committee, I am submitting this statement for the record of your hearing on April 19, 1982 regarding the "deductibility of certain expenses incurred by self-employed individuals."

Shaklee Corporation is a direct selling company that markets its Nutritional, Household and Personal Care Products in the home through hundreds of thousands of Independent Distributors in all 50 states as well as internationally.

The direct selling industry has grown enormously in recent years, due in part to the need for families and senior citizens to supplement their incomes and to the desire of many women, to create meaningful and rewarding careers consistent with family raising responsibilities. The convenience and financial rewards of direct selling have also attracted minorities including women, the handicapped, and the elderly, to whom other economic opportunities have not been as readily available.

Our Distributors are independent, small business men and women, the majority of whom conduct their Shaklee business on a part-time basis. Once a Distributor achieves a certain level of sales volume, she becomes a Sales Leader and deals with the company directly. Therefore, the majority of Shaklee Distributors who conduct their business at a limited level do not deal directly with the company.

A Shaklee distributorship is an attractive business opportunity for a wide variety of reasons which are totally unrelated to taxes. We have never promoted nor advocated the promoting by others of the Shaklee opportunity as a "tax shelter" or a "tax savings" business. In fact, in our "Join Us" flyer which promotes the advantages of a Shaklee independent distributorship (attached), "potential tax advantages" is only one out of a list of 22 reasons for joining Shaklee.

We have consistently encouraged sound business practices by all our Distributors, such as maintaining accurate records and filing all business related receipts and cancelled checks so that these items will be readily available at tax time. This is stated in the "Shaklee Sales Manual" which is provided to all our Distributors and in the "Build a Better Rainbow" manual which is available to all Sales Leaders (attached).

In January of each year, Shaklee Corporation files with the IRS and with Distributors who have held the rank of Sales Leader in the previous year, a Form 1099-NEC which reflects all compensations paid them by Shaklee in the previous year. This again reminds them of additional income earned and their responsibility to report it when filing their taxes.

In addition to this we included in the April 1982 edition of "Shaklee News", which is circulated to over 70,000 Sales Leaders and other Distributors, an article entitled "Timely Tax Reminder " (attached). This piece, which again reminded our Distributors of their tax responsibilities, included in part the following:

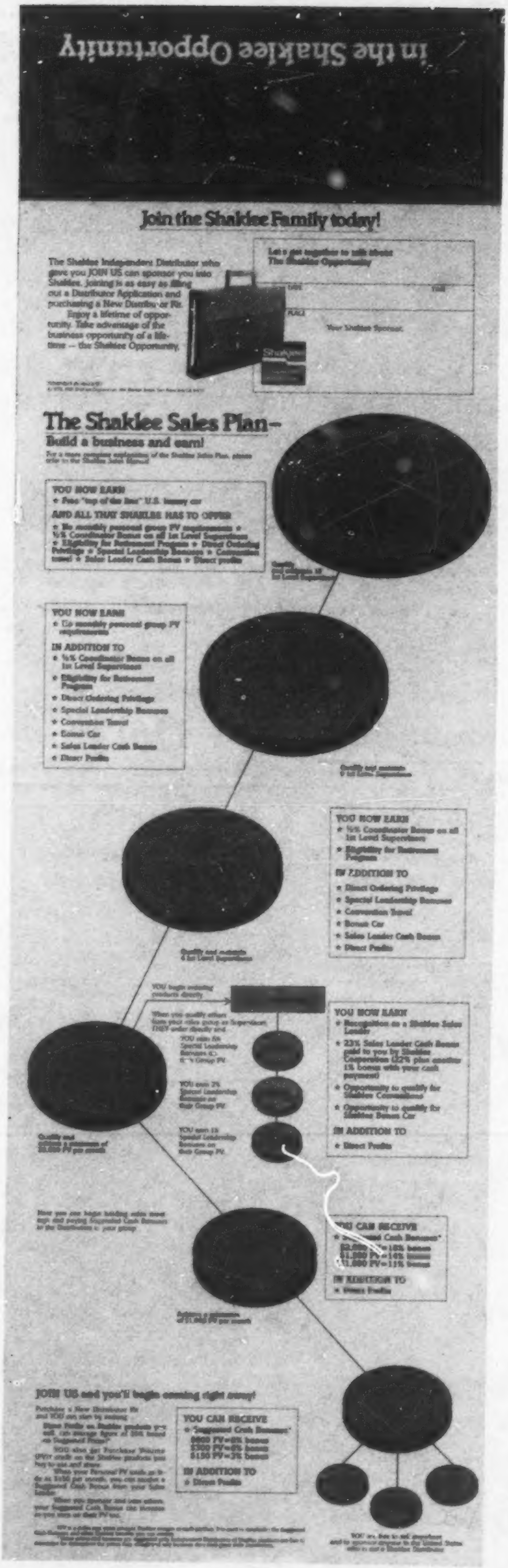
> "...It's a good idea to consult a reputable tax advisor to determine all the legitimate business deductions that may be available to you as an independent contractor, and to ensure proper preparation of your tax returns in full compliance with the law."

Apparently there are a number of tax consultants who are advocating improper tax reporting procedures to self-employed individuals who are not in a position to dispute the advice offered them. The use of these unqualified tax advisors is certainly not encouraged by Shaklee Corporation and is not in our best interest. Misrepresentation or distortion of the Shaklee opportunity and of the sales plan by a Shaklee Distributor could lead to termination.

The problem however, is that the tax laws are extremely complex. Our Distributors need the assistance of capable professionals to file their returns in a manner which complies with applicable law while providing them with all the tax deductions to which they are entitled.

We do not condone excessive tax deductions and we believe that the vast majority of our Distributors are only interested in claiming the tax deductions which are permitted by law.

We support this Committee's efforts to resolve this problem and will continue to provide our assistance in this regard.



in the Shaklee Opportunity

Join the Shaklee Family today!

The Shaklee Independent Distributor who gave you JOIN US can sponsor you into Shaklee. Joining is as easy as filling out a Distributor Application and purchasing a New Distributor Kit.

Enjoy a lifetime of opportunity. Take advantage of the business opportunity of a lifetime — the Shaklee Opportunity.

Let's get together to talk about The Shaklee Opportunity

DATE TIME

PLACE

Your Shaklee Sponsor:

The Shaklee Sales Plan–

Build a business and earn!

YOU NOW EARN
- Free "top of the line" U.S. luxury car

AND ALL THAT SHAKLEE HAS TO OFFER

No monthly personal group PV requirements ✦ ½% Coordinator Bonus on all 1st Level Supervisors ✦ Eligibility for Retirement Program ✦ Direct Ordering Privilege ✦ Special Leadership Bonuses ✦ Convention travel ✦ Sales Leader Cash Bonus ✦ Direct profits

YOU NOW EARN
- No monthly personal group PV requirements

IN ADDITION TO
- ½% Coordinator Bonus on all 1st Level Supervisors
- Eligibility for Retirement Program
- Direct Ordering Privilege
- Special Leadership Bonuses
- Convention Travel
- Bonus Car
- Sales Leader Cash Bonus
- Direct Profits

YOU NOW EARN
- ½% Coordinator Bonus on all 1st Level Supervisors
- Eligibility for Retirement Program

IN ADDITION TO
- Direct Ordering Privilege
- Special Leadership Bonuses
- Convention Travel
- Bonus Car
- Sales Leader Cash Bonus
- Direct Profits

YOU begin ordering products directly

YOU earn 2% Special Leadership Bonuses on their Group PV

YOU earn 1% Special Leadership Bonuses on their Group PV

YOU NOW EARN
- Recognition as a Shaklee Sales Leader
- 23% Sales Leader Cash Bonus paid to you by Shaklee Corporation (22% plus another 1% bonus with your cash payment)
- Opportunity to qualify for Shaklee Conventions
- Opportunity to qualify for Shaklee Bonus Car

IN ADDITION TO
- Direct Profits

YOU CAN RECEIVE
- Suggested Cash Bonuses*

$2,000 PV = 18% bonus
$1,000 PV = 14% bonus
$1,000 PV = 11% bonus

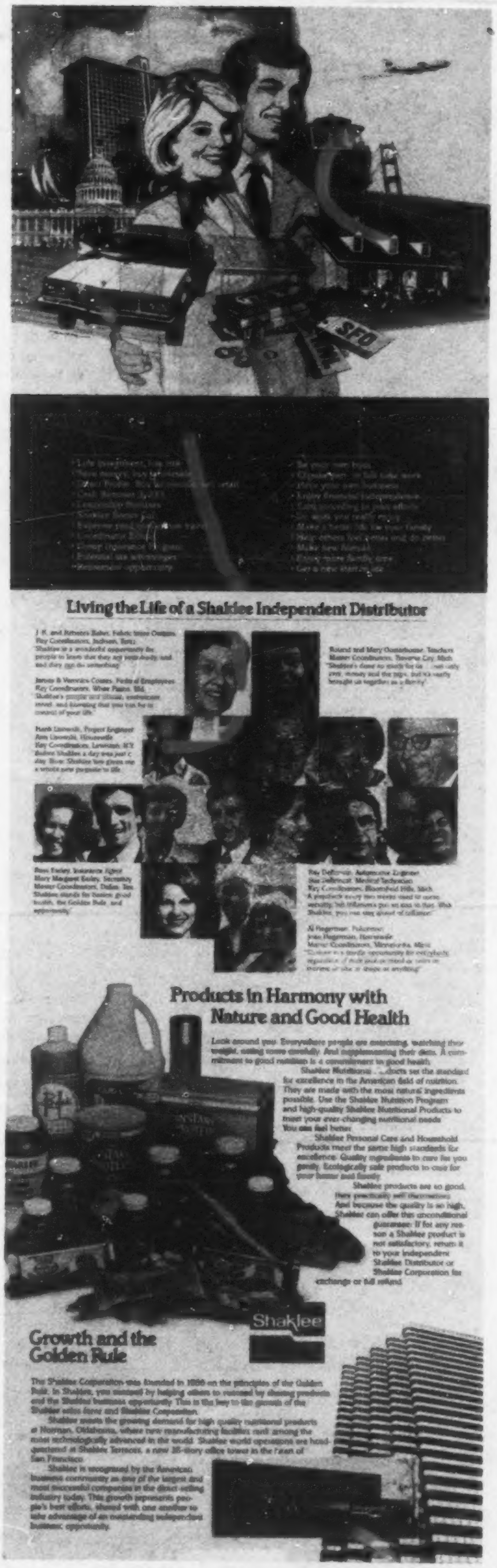
IN ADDITION TO
- Direct Profits

JOIN US and you'll begin earning right away!

YOU CAN RECEIVE
- "Suggested Cash Bonuses"

$600 PV = 8% bonus
$300 PV = 6% bonus
$150 PV = 3% bonus

IN ADDITION TO
- Direct Profits



- Life investment, low risk
- Save money, buy wholesale
- Direct Profits: [illegible]
- Cash Bonuses [illegible]
- Leadership Bonuses
- Shaklee Bonus [illegible]
- Expense paid [illegible] travel
- Coordinator [illegible]
- Group insurance program
- Potential tax advantages
- Retirement opportunity

- Be your own boss
- Opportunities: full or part time work
- Build your own business
- Enjoy financial independence
- Earn according to your efforts
- Do work you really enjoy
- Make a better life for your family
- Help others feel better and do better
- Make new friends
- Enjoy more family time
- Get a new start in life

Living the Life of a Shaklee Independent Distributor

J. R. and Rebecca Baker, Fabric Store Owners, Key Coordinators, Jackson, Tenn.: "Shaklee is a wonderful opportunity for people to learn that they are somebody and that they can do something."

James & Veronica Coates, Federal Employees, Key Coordinators, White Plains, Md.: "Shaklee's people and ideals, enthusiasm, travel, and knowing that you can be in control of your life."

Frank Lisowski, Project Engineer, Ann Lisowski, Housewife, Key Coordinators, Lewiston, N.Y.: "Before Shaklee a day was just a day. Now, Shaklee has given me a whole new purpose to life."

Roland and Mary Oosterhouse, Teachers, Master Coordinators, Traverse City, Mich.: "Shaklee's done so much for us ... not only cars, money and the trips, but it's really brought us together as a family."

Russ Easley, Insurance Agent, Mary Margaret Easley, Secretary, Master Coordinators, Dallas, Tex.: "Shaklee stands for honesty, good health, the Golden Rule, and opportunity."

Ray [illegible], Automotive Engineer, Sue [illegible], Medical Technician, Key Coordinators, Bloomfield Hills, Mich.: "A paycheck every two weeks used to mean security, but inflation's put an end to that. With Shaklee, you can stay ahead of inflation."

Al Hagerman, Policeman, Jean Hagerman, Housewife, Master Coordinators, [illegible], Minn.: "Shaklee is a terrific opportunity for everybody, regardless of their [illegible]"

Products in Harmony with Nature and Good Health

Look around you. Everywhere people are exercising, watching their weight, eating more carefully. And supplementing their diets. A commitment to good nutrition is a commitment to good health.

Shaklee Nutritional Products set the standard for excellence in the American field of nutrition. They are made with the most natural ingredients possible. Use the Shaklee Nutrition Program and high-quality Shaklee Nutritional Products to meet your ever-changing nutritional needs. You can feel better.

Shaklee Personal Care and Household Products meet the same high standards for excellence. Quality ingredients to care for you gently. Ecologically safe products to care for your home and family.

Shaklee products are so good, they practically sell themselves. And because the quality is so high, Shaklee can offer this unconditional guarantee: If for any reason a Shaklee product is not satisfactory, return it to your independent Shaklee Distributor or Shaklee Corporation for exchange or full refund.

Shaklee

Growth and the Golden Rule

The Shaklee Corporation was founded in 1956 on the principles of the Golden Rule. In Shaklee, you succeed by helping others to succeed by sharing products and the Shaklee business opportunity. This is the key to the growth of the Shaklee sales force and Shaklee Corporation.

Shaklee meets the growing demand for high quality nutritional products at Norman, Oklahoma, where new manufacturing facilities rank among the most technologically advanced in the world. Shaklee world operations are headquartered at Shaklee Terraces, a new 38-story office tower in the heart of San Francisco.

Shaklee is recognized by the American business community as one of the largest and most successful companies in the direct-selling industry today. This growth represents people's best efforts, shared with one another to take advantage of an outstanding independent business opportunity.

19. In some cases, you may not be required to pay tax. For example, you may arrange for a "resale permit" or "tax number," if your state has such a system, or you may be selling products out-of-state, or to tax exempt organizations such as churches, federal government agencies or non-profit groups. Ask your Sales Leader about exemptions, since sales tax laws vary from state to state. If applicable, enter your reason here.

20. Enter the names of your sponsor.

21. Enter your Personal PV goal here. Talk it over with your Assistant Supervisor or Supervisor first to determine a reasonable goal for you. As the month progresses, keep a running total of your PV from each order to see how you're measuring up to your goal.

22. Use this space to explain adjustments, make special delivery arrangements, ask for special packaging, etc.

As soon as you have completed your Distributor Purchase Order, check it for accuracy. Then take it to the Assistant Supervisor or Supervisor you are ordering from and pick up your products. If you live some distance from your Sales Leader, mail him the purchase order and wait for your products to be shipped. Or perhaps you have an arrangement for phoning orders in to speed up delivery.

As soon as you receive delivery, check all the products against your order, and inspect them for damages. If there is any discrepancy, notify your Sales Leader immediately to resolve it.

Break your products down into individual customer orders, and package them neatly so that they won't be soiled or damaged, and so that you can deliver them conveniently. You may want to order some of the special product bags offered by Shaklee to do this. Mark each order clearly with the customer's name.

Now, you are ready to deliver the products. When you have several deliveries to make on the same outing, plan your route to avoid wasted time and back-tracking. Call ahead to each customer to remind him or her of your appointment. Use this call to ask if there is any other product sample or literature you can bring, then include something extra even if your customer can't think of anything.

Deliver the products, collect payment, (if you haven't already done so) politely introduce other products, look for an opportunity to sponsor, and leave with a promise to keep in touch. Deposit your customers' payments promptly in your Shaklee bank account.

While you're out, pay a visit to a good stationery or business supply store. Browse around and you'll probably spot several things that will make your new business easier to run and less time-consuming: carbon paper, paper clips, staples, tape, file cards, folders, calendars, etc.

That same store, or local print shop, can also make you a rubber stamp with your name, address, phone and "Independent Shaklee Distributor." This stamp will go a long way toward relieving the case of writer's cramp you may be experiencing. Use it on forms, envelopes and all product literature you send out.

Make sure you save the receipts from anything you buy specifically for your business. File receipts away in a safe place, along with your canceled checks, until it's time to do your income tax.

After you have delivered your first product orders, save all of the yellow receipts (your copy of each customer's order). You can use these receipts to set up a good system for recording and organizing customer information.

Why are customer records important to you? Good record-keeping often means the difference between success and failure, especially in a business built on customer service. With a good system, you can find information you need at a glance. So, if one of your customers has a question about a previous order, or you need to determine which customers are ready for a follow-up call, you don't have to waste time digging through a pile of disorganized papers: you've got the information at your fingertips.

Keeping records doesn't have to be time-consuming, expensive or frustrating, either. You can set up a simple system for organizing customer information for just a few dollars and about half an hour of your time.

4. Post a freight policy. Who pays for freight when an out-of-town Distributor orders products? Some Sales Leaders always pay freight. Others pay it when the order is over a certain dollar amount. Some split the cost with Distributors. Some will pay freight for Distributors, but turn over the freight cost when the Distributors become Assistant Supervisors.

Decide for yourself how you want to handle it, then be consistent.

5. Pay bonuses on time. You should pay them within two days of receiving your own bonus. Your Distributors are counting on you!

Evaluate Your Recordkeeping System

Keeping simplified, accurate records or books is one of the hardest things for some newer Supervisors to deal with—often because it appears more difficult than it is. Still, while it doesn't have to be hard, it does have to be done. In fact, it's important enough that it can make or break a Shaklee business.

Why Is Recordkeeping Important?

1. You must have accurate records at tax time. The IRS wants details—in writing! Without records, you may not be able to claim your rightful deductions. It almost goes without saying that complete records are a must if you're ever audited.

2. Your up-to-date records assure that the people in your group are being properly taken care of: bonuses paid, orders credited, Distributor Applications processed, etc.

3. Finally, your records show you where you stand, at any given moment, in relation to your goals.

Timely Tax Reminder

As a distributor of Shaklee products, you are an independent contractor and responsible for reporting and paying taxes on your income. That includes federal, state, and local income taxes, Social Security taxes and others.

You may also have legitimate business deductions as an independent contractor, and you may be required to file information returns (Form 1099 NEC) for members of your group.

It's a good idea to consult a reputable tax advisor to determine all the legitimate business deductions that may be available to you as an independent contractor and to ensure proper preparation of your tax returns in full compliance with the law. ●

Look What We've Attached to *Shaklee News!*

It's the Presentation Guide to the *In Harmony with Nature* Nutrition Series

Here is the key to the whole "Nutrition Series," and we've included it in this issue of *Shaklee News* free of charge.

You've no doubt seen the Series, and you probably even own components of it, so you know how effective it is as a business builder and sponsoring tool.

The Presentation Guide describes the variety of pieces available and suggests how you can make the Series even more useful. Check it to make sure you have all of the components you need, and how to make best use of them.

Or, if you already have the Guide, pass this copy on to an up-and-coming Distributor. You (and the Distributor) will be glad you did.

Remember, the Presentation Guide cannot be purchased separately. Except for this complimentary copy, it is available only as a part of the Flip Chart. ●

Let's Get Technical –

See Attachment to This Issue of *News*

Errors, changes, updates — these are the demons that plague all publications no matter how hard we strive for perfection. Attached to this issue of *Shaklee News* you'll find a brief sheet of last-minute revisions for the new *Technical Notebook*. Please incorporate them into the notebooks you've purchased. We appreciate your cooperation — and your interest in this fine learning and sharing tool. ●

Diary of a Basic-H Researcher — Part II

Our story to date

After establishing the need for a reliable soil wetting agent, the Shaklee Corporation appoints Drs. C. Dean Piper and Edwin C. Seim of California Polytechnic State University, San Luis Obispo, to conduct preliminary tests with ***Basic-H*® *Concentrated Organic Cleaner*** to determine its soil wetting properties.

Field tests are conducted on three soils with a history of poor water penetration in California's agricultural belt. Two devices constructed by the Basic-H research team are instrumental in conducting the tests: a flood-basin infiltrometer (simulates flood irrigation) and the overhead-spray infiltrometer (simulates a sprinkler system or rainfall).

The results of tests done on the first group of soils are promising and the research continues full speed ahead on a second group of soils. *Our story continues.*

October 1979

"Shakedown" trials on campus with the overhead sprinkler infiltrometer prove that it is up and running. The staff prepares for the next phase of the research which will be conducted in the San Joaquin Valley.

A two-ton enclosed project van unit is outfitted to establish a completely self-contained unit that can be driven from one field location to another. The van unit provides secure storage for equipment when left at the site overnight, and allows the field crew to move into any given field and conduct studies without having to be connected to an on-site source of water or electricity.

The van's packing list includes: 1) a 1,500-gallon water tank, plumbed so that water can be added or drained from the tank without the field crew entering the truck, 2) a self-contained water pressure system for providing water to the overhead (sprinkler) unit, 3) a large-volume gas-powered pump for filling the tank when needed, or pumping the water from the tank out into the field if gravitational flow is not sufficient, and 4) an electrical generator.

With the van unit packed and ready to go, it's on to the San Joaquin Valley to retest sandy clay loam soil.

November 1979

A four-week study with sandy clay loam soil shows positive results for use of Basic-H to improve water infiltration into soils. These results are *very* promising.

Jan. 1980 – March 1980

Data collected during summer and fall 1979 are processed and written up.

A second year of study is proposed and accepted by the Shaklee Corporation to complete research on the initial soils as well as a second group of soils.

April 1980

Feasibility study results reported to Shaklee Corporation.

June 1980

Two additional flood infiltrometers are built to accommodate the expanded study.

July 1980 - Dec. 1980

Research continues on the first three soils tested, but three additional soils are added. The research study is expanded to include sandy loam soil in the Salinas Valley, silty clay loam soil in the Sacramento Valley, and silty clay soil in the Imperial Valley. A variety of crops are grown on these soils including broccoli, turf grass, and alfalfa.

The researchers set up a circuit route, moving from one site to another on a weekly basis to check each soil on a three-week, six-week, and nine-week schedule. The pace is quick and intense. A driving average of 500 miles a week between test sites is recorded on the truck odometer.

In the San Joaquin Valley, the temperatures frequently reach 115 degrees Fahrenheit and over. To cool off, the staff jumps into the icy Kings River which is fed from lakes in the Sierra Range.

February 1981

Drs. Piper and Seim present the second year's research results to the Shaklee Corporation. These data are used to develop and write the Basic-H Concentrated Soil Conditioner Information Guide.

June 1981

The research procedures of the previous summer are repeated to obtain data for the 1981 growing season. The 1981 results confirm that Basic-H Concentrated Soil Conditioner is dramatically effective in promoting infiltration of water into soils.

December 1981

All the facts are in! The research data are confirmed.

January 1982

This now means that Basic-H Concentrated Soil Conditioner: 1) helps increase the rate at which water penetrates soils, 2) makes water wetter, overcoming water repellency, 3) promotes maximum water utilization by reducing runoff and loss by evaporation, 4) assists drainage in areas where standing water may otherwise accumulate, 5) permits more uniform water penetration, thereby reducing dry spots.

But we aren't closing the books yet on this one. Further research will be conducted with Basic-H Concentrated Soil Conditioner to investigate additional influences on soil and water relationships.

A researcher's work is never done. ●

by Catherine Wurdack

Contact Field Communications, *Not* Dr. Piper!

If you have questions regarding Basic-H Concentrated Soil Conditioner, **please do not under any circumstances contact Dr. C. Dean Piper** at California Polytechnic State University, San Luis Obispo.

Your written inquiries should be directed to Field Communications. They will be happy to help you. Thank you for your cooperation. ●